

REPORTS OF INCOME TAX CASES

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Hon'ble Shri Justice B. MALIK, M.A., LL.B.

**OF THE HON'BLE SOCIETY OF LINCOLN'S INN., BARRISTER-AT-LAW,
CHIEF JUSTICE, ALLAHABAD HIGH COURT (NOW RETD.)**

VOL. IV

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REPORTS
OF
INCOME TAX CASES

DECIDED IN
THE HIGH COURTS OF JUDICATURE AND CHIEF COURTS
IN BRITISH INDIA

EDITED BY
P. R. SRINIVASAN, M.A., B.L.
Advocate, High Court, Madras

VOL. IV



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INCOME TAX CASES.

(308) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice Chatterjî and Mr. Justice Fazal Ali.

(6th May, 1929.)

A. H. Forbes

Assessee.*

v.

The Commissioner of Income-tax, Bihar and Orissa . . Referring Officer.

Income-tax Act (XI of 1922), Secs. 8, 10, 12 and 24—Interest from Government Securities—Commission paid to Bank for realisation of interest—If deductible in computing assessable interest.

Under Sec. 8 of the Income-tax Act, income-tax is payable by the holder of Government Securities on the whole of the interest receivable therefrom without any deduction of the commission paid by him to his Bank for the realisation of the interest. The commission so paid cannot be deducted or set off under Secs. 10, 12, or 24 of the Income-tax Act.

Application [Mies. Judicial Case No. 39 of 1929] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Behar and Orissa, to state a case for the opinion of the Court.

K. P. Jayaswal and Mohdi Imam, for the Assessee.

JUDGMENT.

FAZL ALI, J.:—This is an application asking this Court to call upon the Commissioner of Income-tax to state a case under section 66 of the Income-tax Act, the question raised being as to whether the petitioner, who has paid to his bankers certain commission at the rate of a quarter per cent for the realisation of interest on the Government securities held by him, is or is not entitled to claim that the amount paid to the bankers by way of commission should be deducted from the interest receivable on those securities and that the income-tax should be charged only on the sum actually received by him. The view taken by the Income-tax Commissioner is that section 8 of the Income-tax Act is conclusive on the point and that the tax is payable not on the amount actually received by the assessee but on the interest receivable by him on the securities held by him. Now, the language of section 8 is so clear that it is difficult to hold that the view taken by the Income-tax Commissioner is not correct.

It was however contended that the present case may come under section 10 or section 24. Section 10 clause (1) runs as follows:—"The tax shall be payable by an assessee under the head "business" in respect of the profits or gains of any business carried on by him." Now, in this case the securities are held by the petitioner as investments and it is not his case that he carries on the

* A. I. R. (1929) Patna. 419.

business of buying or selling securities in the same way as one deals in stocks and shares in the share market. It is true that in his application to the Commissioner of Income-tax the petitioner contended that his case came under section 10 of the Income-tax Act but the contention was based upon a curious reasoning which is to be found in the following passage in that application:—"That having little time to look after my *pecuniary investments* or to draw the interest and dividends receivable therefrom on due dates, I have been constrained to enter into business relations with the said Banks and Agents in accordance with their rules and practice, so as to obtain the aforesaid interest and dividends and to have proper accounts of them, and in return I have to remunerate them by an allowance of commission both on the sums realised and the sums invested or paid out by them, they submitting the accounts at the close of the financial year by statements of account, or by balancing the entries in the Pass Book where such have been supplied by them." Now, this is obviously a very laboured way of trying to bring the case under section 10 of the Income-tax Act. In fact as has been pointed out by the Commissioner of Income-tax there are six heads of income in the Act; namely, (1) salaries, (2) interest on securities, (3) property, (4) business, (5) professional earnings and (6) other sources. The assessee when submitting his return has to state under which and how many of these heads he derives his income. In this particular case the return submitted by the petitioner shows that he described his earnings on securities under the head of "Interest on securities." This being so, it is clear that section 8 will apply to the case and the tax will be levied on the amount receivable by the petitioner as interest on security and not on the amount which actually came into his hands after deducting the commission payable to the bankers.

The next question is as to whether any relief can be given to the petitioner under section 24 of the Income-tax Act. Section 24 clause (1) runs as follows:—"Where an assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year". Now, in the first place I do not think that the payment of a commission to the bankers by the assessee himself can without stretching the language be held to constitute loss of profits or gains in the sense the expression has been used in section 24. Then again all that section 24 says is that the loss of profits under *one of the heads* may be set off against the income, profits or gains under *any other head* in a particular year. It does not provide that the assessee is entitled to claim a deduction of the expenses incurred by him in collecting his income under any particular head from the gross income under that head. Such a deduction may be claimed only under sections 9, 10, 11 and 12 in appropriate cases. But as I have already said the present case does not fall under any of these sections, but falls directly under section 8 of the Income-tax Act. Besides, the petitioner did not urge in the application before the Income-tax Commissioner that his case came under section 24 of the Income-tax Act; it is for the first time that the point has been raised in this Court.

The decision of the Commissioner seems to be correct and the application is accordingly rejected.

It may however be observed that if the case was to be decided on equitable considerations alone the petitioner had no doubt a good case; but the case has to be decided with reference to the law in force and all I can say is that this case brings into prominence one of the obvious deficiencies in the present law.

CHATTERJI, J.:—This is an application for calling upon the Income-tax Commissioner to make a reference under section 66 (2) of the Income-tax Act on the following point of law:—"Whether the cost of collection in respect of

securities and debentures is deductible under sections 8, 10, or 12 or 24 of the Income-tax Act."

The petitioner holds Government securities of the value of over Rs. 21,00,000 and debentures and shares of the value of several lacs. The case for the petitioner is that to obtain and collect interest thereon the said securities are placed with the Imperial Bank of India which collects the interest and renders an account thereof to the petitioner charging a commission of 1¼ per cent. The petitioner claims that no income-tax ought to be charged on the commission so paid to the Bank for realization of interest and Government Promissory Notes and debentures and that the Commissioner of Income-tax who refused his prayer may be called upon to state a case for the opinion of this Court.

Section 6 of the Income-tax Act specifies the heads of income chargeable to income-tax. The heads are six in number, (i) Salaries, (ii) Interest on securities (iii) Property (iv) Business (v) Professional earnings (vi) Other sources. Section 7 deals with salaries; section 8 with interest on securities; section 9 with property; section 10 with business; section 11 with professional earnings and section 12 with other sources. These heads are mutually exclusive of one another. The item regarding which this petition has been moved is dealt with in section 8. It provides that the tax shall be payable by an assessee in respect of interest receivable by him on any security of the Government of India or of a Local Government, or on debentures or other securities for money issued by or on behalf of a local authority or a company. This section does not show any deductions to be made as in the case of the other items. As to property clause (6) of section 9 (1) allows deduction in respect of collection charges. In business the assessment is to be made under Sec. 10 in respect of profits or gains computed after making certain allowances. In professional earnings computation is to be made under Sec. 11 after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains. Similarly section 12 provides for an allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning income, profits or gains under the head "Other sources." If really the legislature intended that any deduction is to be made for collection charges in respect of interest on securities or debentures, I have not the slightest doubt that some provision would have been made to that effect in the Act. *Prima facie*, therefore, the assessee is bound to pay income-tax upon all the interest receivable by him.

It is however, contended that the transaction is a business and, therefore, in calculating the profits thereon, collection charges must be deducted; but no such case has been made in the petition made before this Court. It is true that it was contended before the Income-tax authorities that the dealings are in the nature of business; but all that was said was that the investment in the Government Promissory Notes is a business, not that he purchases or sells the shares as a business dealing. Then the profit of a trade or business as laid down by Lord Herschell in *Russell v. Aberdeen Bank*(1), is the surplus by which the receipts from the trade or business exceed the expenditure necessary for the purpose of earning these receipts. Therefore, if it be treated as a business what can be deducted is the expenditure necessary for the purpose of earning these receipts. Now if the petitioner collected the interest himself then no Bank commission was required to be paid. Consequently, it cannot be maintained that the commission paid to the Bank for cost of realization is an item of expenditure necessary for the purpose of earning a receipt on account of interest. It is next urged that the case falls within the provision of section 12, but it deals with "other sources." This expression means sources other than the preceding five heads as specified in section 6. When there is a specific head for interest on

(1) 2 Tax Cas. 821 at page 827.

securities and a specific section providing for this head, I do not think that the residuary section 12 can be called into aid.

It is lastly urged that the case would fall at least under section 24 of the Income-tax Act, where it is provided that if any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set-off against his income, profits or gains under *any other head* in that year. I do not see how the commission paid to the Bank for realisation of interest can be said to be a loss of profits or gains sustained by the assessee. When a person carries on a trade or profession, if he actually incurs a loss from the same the figure adopted under that head in arriving at the aggregate amount of the income chargeable to tax would be nil, and not a minus sum. It is, therefore, that this statutory provision is made that a loss under one head of income may be charged against profits under another in the same year. The provision that the loss is to be set off against the income, profits or gains under any other head makes the position quite clear. Assuming that the commission paid to the Bank for collection is to be taken as an amount of loss section 24 cannot be made applicable to such a condition, because, what the petitioner prays is that the payment of commission (treating it as loss) is to be set off against the income of the same particular head. In my opinion the whole of the interest receivable by the petitioner is an assessable income within the meaning of section 4 of the Income-tax Act and there is no reason why an allowance should be made for the commission paid to the Bank in arriving at the assessable income. The petitioner has clearly failed to show that he is entitled to any such exemption, as is claimed by him. The petition is accordingly rejected.

(309)

IN THE CHIEF COURT OF OUDH.

Before Justice Sir Luis Stuart and Mr. Justice Raza.

(10th May, 1929).

Nawab Muzaffar Ali Khan

.. Assessee.

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act (XI of 1922), Secs. 22 (4) and 23 (4)—Notice to produce accounts and evidence—Production of false accounts—Assessment under Sec. 23 (4), legality of—Rejection of accounts by Income-tax Officer—If a question of law.

Where accounts, documents or evidence called for by the Income-tax Officer and produced by the assessee intentionally falsify the income, it is open to the Income-tax Officer to make an assessment under Sec. 23 (4) of the Act as for failure to comply with all the terms of the notice under Sec. 22 (4).

The question whether the evidence before the Income-tax Officer was sufficient to justify him in rejecting the assessee's account is a question of fact and not one of law.

Case [Civil Reference No. 2 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

The assessee, Nawab Muzaffar Ali Khan, carries on money-lending business and advances loans at rates varying from 12 to 24 per cent. per annum.

On April 2, 1928, the Income-tax Officer, Lucknow, served on the assessee a notice under section 22 (2) of the Income-tax Act requiring him to submit, on or before May, 4 1928, a return of his total income in the "previous year."

The assessee filed no return of income in 1925-26 (the first year of his assessment) and 1926-27 and was assessed in an income of Rs. 3,000 and Rs. 9,000, respectively, his receipts from interest having been estimated at Rs. 2,000 and Rs. 8,000. In 1927-28 he filed a return for Rs. 2,293, including Rs. 192 from pension, Rs. 349 from property, and Rs. 1,752 from interest, but as he failed to produce his books or prove his return to be correct he was assessed in a sum of Rs. 10,192 including Rs. 9,000 from interest. For the current year he returned his income as follows:—

	Rs.
Pension	.. 192
Property	.. 828
Interest	.. 1,697
	<hr/>
Total	.. 2,717
Less	.. 1,634
	<hr/>
Total	.. 1,083
	<hr/>

The Income-tax Officer did not accept the return and issued on May 10, 1928, a combined notice under sections 22 (4) and 23 (2) requiring the assessee to produce, on May 16, 1928, all the accounts specified in the notice, namely, the cash book and the ledger for the money-lending business and the register for the collection of rents on his property.

On May 16, 1928, the assessee appeared before the Income-tax Officer and produced one book, the only account he had ever produced since his assessment to income-tax began in the year 1925, in which interest received was alleged to have been entered. The Income-tax Officer checked this book with the list of outstandings which the assessee had filed along with the return of income and found that the income stated in the return tallied with the total amount shown in the book. But the book itself was only a rough account and the Income-tax Officer decided to make further inquiries before completing the assessment. During his examination of the accounts of other firms the Income-tax Officer came to know that the assessee had received certain items of interest from one L. Madan Lal which had not been noted in the books produced. The assessee was again asked to appear at the Income-tax Office on September 12, 1928, and the Income-tax Officer put to him the definite question whether he had received this item of interest in the previous year. In reply the assessee stated that "I have no money-lending business with Madan Lal, son of Kunj Behari Lal Rastogi. I had before, but have no dealings from April 1, 1927. My son has dealings with Madan Lal. I cannot say without looking into my accounts whether I received any interest from Madan Lal after April 1, 1927. The accounts produced by me are quite correct. They do not include any amount received as interest from Madan Lal". He, however, wanted time until the following day to reply to the question definitely after looking into his papers. On the next day, i.e., on September 13, 1928, the assessee produced another rough book in which interest received from L. Madan Lal was shown. As these sums were omitted from the list filed, the Income-tax Officer held it to have been proved that that list was incomplete. He, therefore, rejected the accounts and assessed the income from interest at Rs. 9,000, the same as in the preceding year.

The assessee then appealed to the Assistant Commissioner, who agreeing with the Income-tax Officer, dismissed the appeal.

The assessee now demands a reference to the Honourable Chief Court on the so-called points of law set forth by him as follows:— (1) If the assessee submits the return and also files the memorandum of accounts but by mistake omits to enter in the return one item, should the Income-tax Officer assess him on the income returned, *plus* the missing item, or can he assess arbitrarily? (2) Can the Income-tax Officer under such circumstances simply repeat the previous year's assessment made under section 23 (4) instead of determining the total assessable income and assessing accordingly as required by section 23 (3)? Both these issues in the form in which the assessee has framed them beg a question of fact inasmuch as the assumption is made that the omission was accidental. Admittedly the Income-tax Officer was not able to satisfy himself whether the omission was accidental or intentional for the purpose of initiating proceedings for the infliction of a penalty under section 28 because no regular account books had been maintained by the assessee. At the same time he held that the rough accounts produced by the assessee had been vitiated by a proved omission and could not be relied on to disclose the assessee's true income. He, therefore, framed an estimate as he was entitled to do. The question of law which arises is—Was the evidence before the Income-tax Officer sufficient to justify him in rejecting the accounts of the assessee?

The Commissioner is of opinion that having regard to all the circumstances set forth in this statement, the question should be answered in the affirmative.

JUDGMENT.

This is a reference to the Chief Court under Sec. 66, Cl. (2) of the Indian Income-tax Act (Act XI of 1922). The facts are stated in the order of reference. It is sufficient to note here that the assessee in 1925-26 filed no return. His assessment was then made under the provisions of Sec. 23 (4). In 1926-27 he also filed no return. His assessment was again made under Sec. 23 (4). In 1927-28 he filed a return of Rs. 2,293. He was called upon to produce accounts under the provisions of Sec. 22 (4). As he did not do so his assessment was again made under Sec. 23 (4). In 1928-29 he made a return and produced accounts but the Income-tax Officer considering that the income disclosed in the accounts had been intentionally understated proceeded to assess on the 1927-28 figures with a slight addition. The assessment was said to be made under Sec. 23 (3). It is in regard to that assessment that this reference has been made.

Under the Act the procedure is as follows. The assessee when called on must make a return. If the Income-tax authorities are not satisfied with the entries in the return they can call on the assessee to produce such accounts or documents or such evidence as they may require. If those accounts or documents or evidence furnish sufficient material for an assessment, the assessment should then be made under Sec. 23 (3), but if those accounts or documents or evidence do not furnish sufficient material for an assessment and in particular if they so far from revealing the income intentionally falsify the income, it is open to the Income-tax Officer to make an assessment under Sec. 23 (4), for the assessee has failed to comply with all the terms of the notice. The Income-tax authorities can then further take action under the provisions of Sec. 28 of the Income-tax Act, or under Sec. 177 of the Indian Penal Code against the assessee. This is the procedure.

The question remains whether a High Court has any jurisdiction to interfere with the decision of the Income-tax authorities as to whether there has

been a compliance with the terms of the notice. In our opinion this is not a question of law but a question of fact. We have been asked by the Commissioner of Income-tax to determine whether the evidence before the Income-tax Officer was sufficient to justify him in rejecting the accounts of the assessee. We do not consider that this is a question of law. It is a question of fact; and as it is a question of fact we can express no opinion on it. As this reference was made at the instance of the assessee we direct that he pays the costs of the reference. We fix the costs of the Government Advocate at Rs. 100.

(310) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Niamat Ullah.

(14th May, 1929).

Messrs. Chokhey Lal Murlidhar

.. Assessee.

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Income-tax Act, (XI of 1922)—Hindu Joint family—Members carrying on separate businesses in individual names—Agreement stating the businesses to be separate—Division, if effected.

Where an agreement entered into between the members of a Hindu joint family merely stated that certain businesses carried on by some of the members in their names were the separate businesses of the respective members, each independent of itself with no concern in the assets and liabilities of the others and there was no disclosure therein of any intention on the part of the family members to separate.

HELD, that there was no disruption of the joint family.

Case [Misc. Case No. 88 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

Lala Chokhey Lal is the head of an undivided Hindu family carrying on business at Haldwani in the district of Naini Tal under the name and style of Messrs. Chokhey Lal Murlidhar. The family consists of himself, his brother Lala Murlidhar, his sons Lala Kanhaiya Lal and Lala Ram Ratan, and the minor sons of Lala Murlidhar. The business is carried on at three shops, two of them for the sale of grain and one for that of cloth. One of the grain shops is managed by Lala Chokhey Lal himself as the head of the family and the other by his son Ram Ratan. The cloth shop is managed by the other son Lala Kanhaiya Lal. All the three shops have hitherto been treated as a joint family concern and income-tax has been charged on this basis.

2. On July 13, 1927, Lala Chokhey Lal submitted, on behalf of the undivided Hindu family, a return of his income for the "previous year" accompanied by a petition in which he stated that the return related to the joint family business alone and that Kanhaiya Lal and Ram Ratan who had already for some time previously been carrying on cloth and grain business separately might be required to submit a separate return of their income. In view of the fact that all the three businesses had hitherto been assessed together as a joint family business, the Income-tax Officer, Bareilly, who is the assessing officer in this case, rejected the return and required the assessee by means of a com-

bined notice under sections 22 (4) and 23 (2) to produce the accounts and prove that Kanhaiya Lal and Ram Ratan had ceased to be members of an undivided Hindu family and that they were the sole proprietors of the business which they were carrying on. The relevant accounts for each business were produced, and as regards the question of separation and the separate business of the two sons, the assessee, Lala Chokhey Lal went into the witness-box and stated that he separated from his sons Kanhaiya Lal and Ram Ratan as soon as they attained their majority, that is, judging from their present age, about 12 years ago. At the same time he admitted that no formal partition was made, nor was the ancestral property divided among the several members of the family. All that was done was that a cloth shop was allotted to one and a grain shop to the other son. The reason assigned for the separation was that differences arose among the ladies of the house.

3. In support of the alleged separation some 12 years ago the assessee produced five witnesses and a deed of declaration executed and registered on March 27, 1927. After considering the evidence produced the Income-tax Officer found, as a matter of fact that the assessee, Lala Chokhey Lal, had failed to prove that, as alleged by him, he had separated from his sons Kanhaiya Lal and Ram Ratan as soon as they attained the age of majority some 12 years ago, and his finding was upheld by the Assistant Commissioner. Indeed, his son Lala Kanhaiya Lal, who went into the witness-box himself gave the lie to the statement of his father when he stated that he separated when he opened the cloth shop in the year 1924. Lala Ram Ratan did not go into the witness-box, but the income from the grain business now attributed to him was shown by the assessee as part of the joint family income in the year 1923-24. In these circumstances the assessee had failed to prove that he had separated from his sons some 12 years ago when they attained their majority. As regards the funds with which the business was started, the accounts revealed that the capital was supplied by the joint family business, and the fact that interest was charged on it did not prove that it was the self-acquired property of the sons, because not infrequently the proprietor of a business charges interest on his own capital. Further, it is clear from the accounts that surplus funds are still kept with the joint Hindu family and further requirements met by it. It is not therefore, true to say that Lala Chokhey Lal gave his sons some capital as a loan to start separate businesses of their own. Nor do the accounts show that any part of the capital has been paid back. The accounts of both the businesses are still running, and it is clear what the profit actually was and how it had been disposed of. It is not disputed that the sons live in separate houses and have separate kitchens. But that does not prove that they have separated from the joint Hindu family.

4. The assessee now desires that his case may be referred to the Hon'ble High Court for the decision of the following points of law as propounded by him:—

“2. The facts proved are:—

- (a) That Chokhey Lal, the managing partner of the joint firm consisting of himself and his brother Murlidhar and styled as “Chokhey Lal Murlidhar,” separated his sons Kanhaiya Lal and Ram Ratan Lal on account of a family feud (the relations between their wives and their mother not being good) and gave them some capital as loan to start separate businesses of their own and pay back the capital so advanced with interest from the profits of their respective businesses.
- (b) That the property of Chokhey Lal has not yet been divided by metes and bounds, nor accometes (sic) of the firm going on in the name of Chokhey Lal and Murlidhar have been rendered.

- (c) That the sons carry on their separate business, board and lodge separately, spend separately on their respective families, keep the income of their separate businesses to themselves, and have no concern whatsoever with the income of joint business.

“3. That the question of law involved is whether these sons’ firms should be assessed separately or jointly with the joint business.

“4. That the principles of Hindu Law clearly require that in such a case the businesses of the sons will be deemed to be their separate businesses and should be assessed separately for purposes of income-tax.

“5. That your petitioner’s firm is not an ancestral business and therefore the sons of the petitioner had no interest in it by virtue of their birth according to Hindu Law. All that is proved is that Chokhey Lal and Murlidhar form a joint Hindu family and carry on the business jointly under the name “Chokhey Lal Murlidhar.”

“6. That the Assistant Commissioner while admitting that even members of an undivided Hindu family may have a separate business of their own, still finds without any evidence on the record that the businesses of the sons are joint family concerns in which your petitioners are also interested.

“7. That without any evidence of the fact that the firm Chokhey Lal Murlidhar is ancestral, merely the fact that Chokhey Lal Murlidhar carry on a joint family business does not create any vested right in their sons, although they may be found to be members of the joint family.

“8. That Chokhey Lal being the father is in law entitled to dispose of income of the joint firm Chokhey Lal Murlidhar in any way he likes, because it is his self-acquisition.

“9. Even assuming that the firm Chokhey Lal Murlidhar is an ancestral business, it is settled law that a mere intention to separate is sufficient to change the status of a joint Hindu family. In the present case explicit intention is proved by an agreement to separate, and it has been clearly held (vide 26 A. L. J. R., page 857), that where severance is effected by explicit declaration, the result is decisive and the legal result cannot be affected or controlled by the subsequent conduct of the parties.

“10. That the learned Assistant Commissioner has not considered fully the rulings cited and has taken a wrong view of law and facts.”

5. The first point of law as propounded by the assessee begs the whole question. It is not disputed that if the sons have actually separated and are carrying on their businesses with funds allotted to them as a result of a partition in the family or with funds acquired by them as their self-acquired property, then their income cannot be assessed as a part of the joint family income.

6. But the questions whether they have separated and with what funds they are carrying on the business are questions of fact which the Income-tax Officer and the Assistant Commissioner were alone competent to deal with.

The question whether the joint family business was an ancestral business or the self-acquired property of the assessee was not raised either before the Income-tax Officer or the Assistant Commissioner and cannot therefore be said to arise out of the appellate order. It is therefore unnecessary for me to deal with the further questions whether and to what extent the sons had a vested right in it and the father the right to dispose of the income. The Assistant Commissioner found as a matter of fact that the assessee had failed to prove the separation or the intention to separate, and it followed, as a necessary

corollary of this that the entire income must be assessed as the income of the undivided Hindu family as it had hitherto been assessed.

7. It is not disputed that mere intention to separate is enough to change the status of an undivided Hindu family, but the intention must be expressed clearly and unambiguously.

8. The questions of law that arise in this case and which I refer to the Hon'ble Court are as follows:—(1) Does the deed of agreement dated March 27, 1927 reflect clearly and unambiguously an intention on the part of the members of the undivided Hindu family to effect a separation among them? (2) In all the circumstances of this case, was the Income-tax Officer, Bareilly, wrong in assessing the income from the cloth and grain business carried on by Lala Kanhaiya Lal and Lala Ram Ratan along with the income of the undivided Hindu family and the Assistant Commissioner in taking the view he has taken?

9. The deed of agreement is merely a fabrication for income-tax purposes and has been put forward to escape tax at the appropriate rate. The assessee having failed to prove the separation, the Income-tax Officer was right in assessing the entire income as that of the Hindu undivided family, and the view taken by the Assistant Commissioner cannot be said to be wrong.

10. I am therefore of opinion that both the questions should be answered in the negative.

11. The relevant portion of the statement of the case was sent to the petitioner for observations and representation, if any and, copy of his reply is attached herewith as Appendix E.

APPENDIX A.

Copy of translation of the Deed of Agreement of separation of firms by Chokhey Lal, Murlidhar, Kanhaiya Lal and Ram Ratan, registered at Haldwani on March 30, 1927.

We Chokhey Lal, party No. 1, and Murlidhar, party No. 2, sons of Lala Radha Kishan, and Kanhaiya Lal, party No. 3, and Ram Ratan Lal, party No. 4, sons of Lala Chokhey Lal, Vaish by caste, are residents of Mandi Haldwani, District Naini Tal. Whereas party No. 1, Chokhey Lal, is the head of the family and and party No. 2, Murlidhar, is his real brother. Both of the parties, Nos. 1 and 2, carry on the firm known as "Chokhey Lal Murlidhar." Parties Nos. 3 and 4, on attaining the age of majority, started party No. 3, Kanhaiya Lal, a firm dealing with cloth in his own name and party No. 4, Ram Ratan Lal, a firm dealing with the trade of grain in his own name. Thus the dealings of the above mentioned three firms are separate from each other in every respect and the proprietor of one firm has no concern whatsoever with the assets and liabilities of the other two firms. Each firm is independent of itself. Therefore we the parties concerned have recorded with sound mind and of our own accord and without any pressure or inducement this deed of agreement of separation of firms.

JUDGMENT.

This is a reference under Sec. 66 (2) of the Indian Income-tax Act, 1922 by the Commissioner of Income-tax in the United Provinces. The facts briefly are these. There is a family consisting of a father, two sons, the father's brother and the brother's sons. The father and his brother are Chokhey Lal and Murlidhar and there is a firm styled Chokhey Lal Murlidhar which deal in grain. Chokhey Lal has two adult sons Kanhaiya Lal and Ram Ratan. Murlidhar's sons are minors. Kanhaiya Lal carries on a cloth shop and Ram Ratan

carries on a grain business in another shop. The Income-tax Officer asked for a return of income from Chokhey Lal as the head of the family and he, for the first time, made a return in which the income from the business carried on by his sons was not entered. Chokhey Lal in reply to a question on the point put by the Income-tax Officer said that his sons had been separate for several years and their business was separate. Chokhey Lal produced a document dated the 27th March 1927, besides other evidence in support of separation.

The Income-tax Officer was not at all satisfied that there was a separation and he held that the income-tax should be paid over the aggregate income from the three shops. An appeal to the Assistant Commissioner was unsuccessful. Thereupon Chokhey Lal asked for a reference to this Court.

The Commissioner has framed the following questions for answer by this Court:—(1) Does the deed of agreement, dated March 27, 1927, reflect clearly and unambiguously an intention on the part of the members of the undivided Hindu family to effect a separation among them? (2) In all the circumstances of this case, was the Income-tax Officer, Bareilly, wrong in assessing the income from the cloth and grain business carried on by Lala Kanhaiya Lal and Lala Ram Ratan along with the income of the undivided Hindu family and the Assistant Commissioner in taking the view he has taken?

As regards the document of 27th March 1927, the Income-tax Officer and the Commissioner seem to have come to the conclusion that it was really fabricated for the purposes of avoiding payment of income-tax at a higher rate. That is the opinion which is entertained by the Commissioner of Income-tax and that is a finding of fact which is binding on us. If the document of 27th March 1927, be a purely fictitious transaction, no question of law as framed in question No. 1 arises.

We have however considered the document of 27th March, 1927. We agree with the Commissioner that it does not disclose any intention on the part of members of the joint Hindu family to separate. All that it talks of is the separate character of the three businesses carried on by some of the members of the family. This does not imply a disruption of joint family. That is our answer on the question No. 1.

On question No. 2, our answer is that the Income-tax Commissioner (Officer?) of Bareilly was right in assessing the income in the way he did.

Let a copy of this judgment be sent to the Income-tax Commissioner in reply to his statement of the case. We certify that the learned Government Advocate is entitled to a fee of Rs. 150. He will file the certificate within the usual period allowed.

(311) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Chari and
Mr. Justice Brown.*

(22nd May, 1929).

Somasundaram Chettyar

.. Assessee.

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Income-tax Act, (XI of 1922), Sec. 22 (4)—Non-resident firm with branch in Rangoon—Assessment of Rangoon branch—Jurisdiction to call for other foreign branches' accounts.

The agent of the Rangoon branch of a non-resident firm was called upon under Sec. 22 (4) to produce the accounts of the firm's branches at Alleppey (Travancore State) and Jaffna (Ceylon). The notice was issued as inspection of Rangoon accounts showed that the firm was carrying on business in rice in Rangoon and Akyab by purchasing and exporting rice to Jaffna and that it had also business in Alleppey.

HELD, that the Income-tax Officer had power to call for the accounts.

Case [Civil Miscellaneous Case No. 70 of 1928], stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Burma, in compliance with the order of the High Court.

CASE.

In accordance with the order of the High Court of Judicature at Rangoon in Civil Miscellaneous Case No. 70 of 1928, dated the 3rd January 1929,* the following case is stated for the decision of the High Court under the provisions of section 66 (3) of the Indian Income-tax Act, 1922.

2. The question of law in respect of which I am directed to state a case arises from the assessment of the P. K. N. Chettyar Firm for the year 1925-26 under section 23 (4) of the Act and is as follows:—"Whether, in the circumstances of this case, it was open to the Income-tax Officer to require the production of the books of the Jaffna and Alleppey branches of the assessee; and, if not, whether the failure to comply with such a requisition is a default within the meaning of section 23 (4) of the Act and renders the assessee liable to assessment under that sub-section?"

3. The following are the facts of the case material to the question at issue:—

The partners of the firm, who are taxed through their agent in Rangoon, are two Hindu undivided families resident in the State of Pudukotta (outside British India). Inspection of the Rangoon books of account showed that the firm was carrying on business in rice in Rangoon and Akyab by purchasing and exporting rice to Jaffna (Ceylon) and that it also had business in Alleppey (Travancore State) and in Moovar and Malacca (Straits Settlements).

In order to determine whether there were any other taxable profits of the firm, a notice was issued on 4th March 1926 to the Rangoon agent requiring him to produce on the 24th March 1926 (along with other documents not relevant to the question above) the Jaffna and Alleppey accounts.

This notice contained a warning to the effect that if the Jaffna and Alleppey accounts were not produced the income deemed to arise from these businesses under section 42 (1) would have to be estimated. The Rangoon agent sent the notice to the partners and applied for an adjournment up to the 31st March, which was granted.

On the 31st March, the Rangoon agent (Somasundaram Chettyar) appeared before the Income-tax Officer and filed certain affidavits, but nothing was tendered in respect of the Jaffna and Alleppey accounts. The agent was given time up to the 29th April to produce these accounts. He was at the same time warned that in the event of default the assessment would be made without further notice.

On the 29th April, a pleader appeared for the assessee and filed certain affidavits, one of which was by Nagappa Chettyar, one of the partners, who

* Reported at page 338 *infra*.

stated that there were no transactions between Rangoon and Alleppey in the account year.

As regards Jaffna, he stated that no profits were derived at Rangoon during the accounting period by business connection with Jaffna; he, however, requested that an audited abstract of the Jaffna accounts by competent and recognised auditors might be accepted in place of the books, as it would dislocate the Jaffna business if the accounts relating thereto were removed. The Income-tax Officer agreed to accept audited profit and loss statements and balance sheets and day book extracts relating to the Jaffna and Alleppey businesses and [by a notice under section 22 (4), dated the 4th August 1926], fixed the 30th October 1926, for the production of these documents.

In response to this notice, two communications were received from the partner Nagappa Chettyar, from Madras, urging that the firm was not liable to be assessed on profits arising outside British India. Finally, a hearing was granted to the assessee's advocate from Madras. At this hearing, the Income-tax Officer explained that the profits from business connection between Jaffna and British India (Rangoon and Akyab) were assessable under section 42 (1) read with section 4 (1). But the assessee's advocate adhered to the position that the Jaffna accounts could not be produced.

In the absence of the accounts and documents, and even of the audited profit and loss statement for the Jaffna business, the Income-tax Officer made the assessment under section 23 (4) by his order dated 16th April 1927.

4. My opinion on the question at issue is that the Income-tax Officer had power to require the production of the books of the Jaffna and Alleppey branches and that therefore the second part of the question does not arise. Under the provisions of section 22 (2) of the Act, the assessee who is a non-resident is required to return his total income, that is, his income which accrues or arises or is received in British India [Section 4 (1)] and his income which is deemed to accrue or arise in British India [Section 42 (1).] By section 22 (4) the Income-tax Officer is given the power to require the assessee "to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require." The only qualification to that power is contained in the proviso to section 22 (4) and has no bearing on this case. Now the Income-tax Officer had every reason to believe that the assessee earned an income which was taxable under section 42 (1) and that he could only ascertain the correct amount of this income by a scrutiny of the Jaffna and Alleppey accounts. (It is to be noted that the assessee refused to produce not only the actual books of account but even audited profit and loss statements and day book extracts with which the Income-tax Officer said he would be satisfied). I submit therefore that a limitation on the Income-tax Officer's power such as is contended for by the assessee cannot be read into section 22 (4). In support of this view I refer to *N. D. Radhakishen, & Sons v. Commissioner of Income-tax, Punjab and North-West Frontier Province* (1).

5. In the High Court's order directing this reference, the case of *Duni Chand v. Commissioner of Income-tax, Punjab* (2), is cited as having some bearing on the question at issue in this case. The view taken by the Lahore High Court in the case referred to appears to be that, before an assessee could be held to be in default for the purpose of applying section 23 (4), it should be shown that he is liable to be assessed. In this connection, I note that while the assessee firm in this case at a certain stage of the proceedings denied its liability to be assessed on the profits from its foreign businesses, in its applica-

(1) 2 I. T. C. 345.

(2) 3 I. T. C. 52.

tion to the High Court under section 66 (3) it admits what it describes to be a "special and limited" liability under section 42 (1).

Foucar, for the Assessee.

Gaunt, for the Crown.

JUDGMENT.

The P. K. N. Chettyar Firm, the principals of which are resident in Pudukotta State outside British India, carry on business in Rangoon through their agent. The agent submitted a return of income for the year 1925-26 to the Income-tax Office, and on the 4th of March 1926, the Income-tax Officer issued a notice on him under the provisions of section 22 (4) of the Income-tax Act to produce books of account of the Jaffna and Alleppey branches of the firm. This notice was issued because inspection of the Rangoon books of account showed that the firm was carrying on business in rice in Rangoon and Akyab by purchasing and exporting rice to Jaffna and that it also had business in Alleppey. The books of account not having been produced, the Income-tax Officer made an assessment on the firm under the provisions of section 23 (4), and the question we have now to decide is as to the legality of this assessment.

By an order of this Court the Commissioner of Income-tax has been directed to state the case and refer to this Court the question whether, in the circumstances of this case, it is open to the Income-tax Officer to require the production of the books of the Jaffna and Alleppey branches of the assessee; and, if not, whether the failure to comply with such a requisition is a default within the meaning of section 23 (4) of the Act and renders the assessee liable to assessment under that sub-section. The Commissioner has now stated the case and referred the question to this Court for orders.

The Rangoon agent has presumably been assessed under the provisions of section 42 of the Income-tax Act, and our attention has been drawn to two recent decisions of the High Court of Bombay as to the meaning of the word "agent" in that section. In the cases of the *The Bombay Trust Corporation, Ltd. v. Commissioner of Income-tax, Bombay*(1), and *Remington Typewriter Company (Bombay) v. Commissioner of Income-tax, Bombay*(2), it was held that sections 40, 42 and 43 of the Indian Income-tax Act, 1922, are to be read jointly and not disjunctively, and that in order to make an agent liable under section 42 it is necessary that he should be in receipt of income on behalf of the non-resident for whom he is agent. We understand the contention to be that an agent is not liable save for moneys actually received by him in British India and that therefore books of account from outside British India cannot be necessary for the purposes of assessing income.

We do not consider it necessary to express any opinion on the question raised in the Bombay case, as we are unable to see how it follows as a corollary to the decision in those cases that the agent was not bound to produce the books of account in question in the present case. We do not understand it to be contended that the agent in this case is in receipt of no income on behalf of the non-resident firm. Section 22 (4) is very wide in its terms. It empowers the Income-tax Officer to serve on any person upon whom a notice has been served under sub-section (2) a notice requiring him to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require. The only limitations to the powers of the Income-tax Officer in this respect are that he cannot require the production of any accounts relating to a period more than 3 years prior to the previous year. In the present case the person on whom notice

(1) 3 I. T. C. 135.

(2) 3 I. T. C. 166.

is served is the Rangoon agent of the non-resident firm, but it is the non-resident firm which was being assessed, and it can hardly be contended that it is outside the power of that firm to produce the account books. The Income-tax Officer was of opinion that the books were required to help him to assess the firm to tax, and the section gives the Income-tax Officer full discretion in the matter.

It is impossible for us to hold that the books could not be required and could not give any valuable information as to the amount to which the non-resident firm should be assessed. We can find no authority in the Act for varying the plain meaning of the wording of section 22 (4), or for limiting the power given to the Income-tax Officer by that clause. We are, therefore, of opinion that the Income-tax Officer had the power to call for the account books in question. We answer the first part of the question referred in the affirmative. The second part of the question referred does not therefore arise.

The Chettyar firm will pay the costs of this reference, advocate's fee 5 gold mohurs.

(312) IN THE HIGH COURT OF JUDICATURE AT PATNA.

FULL BENCH.

*Before Sir Courtney Terrell, Kt., Chief Justice, Mr. Justice Ross,
Mr. Justice Wort, Mr. Justice Kulwant Sahay and Mr. Justice Macpherson.
(27th May, 1929.)*

Raja Rajendra Narayan Bhanja Deo . . . Assessee.*
v.

The Commissioner of Income-tax, Bihar and Orissa . . . Referring Officer.

Income-tax Act, (XI of 1922), Secs. 2 (1) (c) and 9—Building occupied by Zamindar—Annual value, if agricultural income—Jurisdiction to determine portion of building as occupied for non-agricultural purposes—Meaning of proviso to section 2 (1) (c)—Mutation fees on transfer of holdings by succession—If exempt as agricultural income.

The Raja of Kanika on an assessment to income-tax claimed exemption under Sec. 2 (1) (c) of the Income-tax Act in respect of the annual value of his residential palace costing about 4 lakhs situate in his Zamindari. In the palace which besides containing the usual accommodation such as drawing room, dining room, etc., had a detached guest house, certain quarters were allotted to certain of his Zamindari staff. The Income-tax Officer rejected the claim to the extent of the sum of Rs. 3,000, determined by him as the proportionate value of the portion of the palace not required wholly and exclusively for agricultural purposes.

HELD, by the Full Bench (Macpherson, J., dissentiente), that on the finding that the building was required by the assessee by reason of his connection with the land, the Income-tax Authorities had no jurisdiction to determine what portion of the building was as a matter of fact required by the assessee in his capacity of receiver of rent or revenue and that the assessee was entitled to claim the entire annual value as agricultural income within the meaning of section 2 (1) (c).

The expression "by reason of his connection with the land" in the proviso to section 2 (1) (c) of the Income-tax Act explains the nature of the class of

* (1929) 9 Pat. 1; A. I. R., (1929) Pat. 449.

persons entitled to exemption and does not confine the exemption to such portion of the building, etc., needed for the purpose of receiving the rent or revenue. The only test is that the receiver of the rent or revenue has to occupy it as a dwelling house by reason of his connection with the land and establishes the relation between himself and his house with the land.

Income in section 2 (1) (c) of the Income-tax Act does not mean income actually earned but includes notional income derived by the owner in occupation.

Mutation fees paid by tenants on the transfer of ryoti holdings upon succession thereto in permanently settled estates are rent or revenue within the meaning of section 2 (1) of the Income-tax Act.

Maharaja of Dharbanga v. Commissioner of Income-tax, 3. I. T. C. 158. Approved.

Case [Misc. Judicial Case No. 120 of 1927], stated under Sec. 66 (3) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, Behar and Orissa in compliance with the order of the High Court, dated 23rd November, 1927.

CASE.

As directed by their Lordships in their order, dated 23rd November 1927, in Miscellaneous Judicial Case No. 120 of 1927, I state below a case on 3 points of law arising out of the order passed on appeal, 30th June 1926, in the assessment made in the year 1925-26 on the income of the financial year 1924-25 of Raja Rajendra Narain Bhanja Deo of Kanika (herein after referred to as the assessee).

2. The first question on which I am asked to state a case may be formulated as follows:—“Whether any portion of the valuation of assessee’s palace at Kanika is taxable, or whether on the other hand the whole valuation of this palace should be exempted as being agricultural income within the meaning of section 2 (1) (c) of the Act”. In my order in review I noted that I would decide this point subsequently according to the decision of Your Lordships in a similar case, which is already before you, but I have been directed to state a case in this assessment as well because it is possible that the other case may be settled and because further this may prove to be a case in which one or other of the parties may take the decision further under legislation which is in contemplation. I presume your Lordships refer to section 66-A of the Act inserted by Amendment Act 24 of 1926, which allows an appeal to the Privy Council and which is already in force.

3. Assessee as stated by his representative who appeared before me yesterday, enjoys an income from agricultural rent amounting to approximately Rs. 2,10,000. His taxable income is approximately Rs. 80,000 and his income from fisheries and other general sources, which is not taxable, or has so far escaped taxation is Rs. 1,00,000. His palace at Kanika was built in the year 1912 at a cost of Rs. 3,00,000 apart from the Zenana quarters, which were subsequently built and which cost another lac. The Manager’s office, which is also situated in Kanika and which is a separate building was built on some date before the year 1902 and houses the general Zemindari staff while the palace proper, a portion of the valuation of which has been taken into consideration for income-tax purposes, accommodates only 7 of the Zemindari staff, practically the whole of the building being used as a residence for the assessee and for visitors. It contains the usual rooms to be found in such a palace including drawing room, dining room, billiard room and bed rooms, while there is a small detached guest house containing one public hall and two bed rooms. The Income-tax Officer

in making this assessment has taken 3,000 as the proportionate valuation of the portion of this palace, which is not required for agricultural purposes.

4. As required I state my opinion on the questions of law raised.

5. If the valuation of the building in question is to be exempted, the following conditions must be fulfilled: (1) it must be owned and occupied by the receiver of rent or revenue from agricultural land, (2) the building must be on or in the immediate vicinity of the agricultural land, and (3) it must be a building which the receiver of the rent or revenue by reason of his connection with the land requires as a dwelling house or store house or other out building. It is admitted that the palace in question is on or in the immediate vicinity of the land, the rent of which the assessee receives, and it is not denied that this building is owned and occupied by the assessee, who is a receiver of rent, but it is the contention of the Department that it is not occupied by him *qua* receiver of rent and that it is not required by him *qua* landlord as a dwelling house, store house, or other out building. The real point at issue is whether the valuation of the whole of the residence of a Zemindar should be exempted from income-tax, regardless of the proportion between that valuation and his income from landed property and regardless further of the proportion which his income from landed property bears to his income from other sources. In this case, assessee's income from rent proper is approximately 50 per cent of his total income and in my view assessee requires or has built this palatial residence not because he requires such a building by reason of his connection with the land but because his total income and high social position demand it. It would, in my view, be straining the law unfairly to hold that the total value of this building is exempt from income-tax by reason of the provision of section 2 (1) (c) of the Act, read with section 4 (3) (viii) and section 2 (1) (c) should be interpreted as giving exemption only to Zemindari Katcheries, Manager's offices and buildings of that nature. It is submitted therefore that this palatial building is not required wholly and exclusively for agricultural purposes and that the question of the valuation of what proportion of the total building assessee should be assessed is a question of fact to be decided in each case, regard being had in coming to a decision to the provisions of the proviso to section 2 (1) (c) of the Act and in particular to the point whether the building in question or the whole of the building is required by reason of the assessee's connection with the land. In this case assessee has not been taxed on the valuation of the out buildings or Zemindari Office, but only on a small proportion of the annual valuation of the palace proper.

6. The next question on which your Lordships have asked me to state a case is "Whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance are covered by the term "Agricultural income" as defined in section 2 of the Income-tax Act of 1922".

7. The term 'tenant' includes both tenure holders and raiyats and under section 14 of the Orissa Tenancy Act (Act 2 of 1913), the landlord is bound to recognize the transfer of a tenure by succession, only provided the transferee pays him a fee amounting to Rs. 2 except in the case of a *Baji aftidar* when the fee shall be Re. 1, while under section 30 of the Act, if a raiyat dies intestate in respect of a right of occupancy it shall, subject to any custom to the contrary, descend in the same manner as other immovable property. In my order in review, when dealing with this point I held that mutation fees realized from occupancy raiyats was an illegal *Abwab* and therefore taxable, while the question whether fees realized on the occasion of transfer of tenures is taxable or not would depend on the finding of Your Lordships in a case already before you and as there was no evidence on record which would enable me to separate the taxable portion of the amount of income shown under this head by the assessee in the explanation

attached to his return of income, viz., Rs. 4,466 from the portion which may not be taxable I refused to interfere with the order of assessment taxing the whole sum as originally shown in the explanation attached to the assessee's return of income.

8. I deal first with the question whether mutation fees paid by tenure holders on succession by inheritance are covered by the term "Agricultural income" as defined in section 2 of the Income-tax Act, 1922. As stated above, under section 14 of the Orissa Tenancy Act of 1913, the landlord is bound to recognise the transfer of a tenure by succession only provided that the transferee pays him a fee amounting to Rs. 2 in certain cases and Re. 1 in others. Assessee's representative alleges that though under the law assessee can realize this amount he as a matter of fact realizes only at the same rates as in the case of transfer of occupancy rights by succession, namely, at the rate of annas two per acre with a minimum fee of annas four and a maximum fee of Re. 1. This transfer fee is not covered by the term "Rent" as defined in section 2 sub-section 1C of the Orissa Tenancy Act and the question is whether it is revenue derived from land which is used for agricultural purposes and the answer to this question would appear to depend on the correct definition of the word "Revenue". This word has been defined in the Oxford Dictionary as, "the return, yield or profit of any land, property or other important source of income; that which comes into one as a return from property or possessions, specially of an extensive kind; income from any source specially of an extensive kind; income from any source but specially when large and not directly earned". If it is held that landlord's fees is money which comes to the landlord by virtue of the fact that he is the owner of the land it is agricultural income, but if this view is correct and the word revenue is taken in this wide sense the result would be to include within the meaning of agricultural income illegal realisations or *Abwabs*, which a landlord realised by virtue of his position as a landlord though these are neither agricultural rent nor revenue. In my opinion the correct way to view these receipts is to hold that they are not rent or revenue derived from land, but are payable by a tenure holder under a liability incidental to the ownership of the tenure.

9. According to the statement of assessee's representative the rate charged is two annas per acre with a minimum fee of four annas and a maximum fee of Re. 1. In the case of each application for transfer regular printed forms are used and a regular file is opened. No raiyat has so far refused to pay this fee—at least not to the knowledge of assessee's representative who appeared before me and has been serving the Estate for twelve years, but on the other hand if a successor by inheritance refuses to pay this fee, the Estate would refuse to recognize him and when he came to pay rent for the holding the receipt would be issued in the name of the deceased occupant, through the payer. In other words, unless this fee is paid the landlord refused to recognize the new raiyat and refused to keep his *Jamabandi* upto date. Assessee's representative does not advance the claim that an occupancy holding is not heritable except with the consent of the landlord. He refused to commit himself on the question whether he could claim this mutation fee in law and on the further question whether steps would be taken to dispossess the succeeding raiyat if he failed to pay the mutation fee; he alleged that if the inheritor does not pay the mutation fee the assessee would refuse to recognize him though he is a tenant in the eye of the law. The position then is this. Occupancy rights are heritable, subject to any custom to the contrary. No such custom has been claimed in the case of this estate and therefore occupancy right should pass to the successor without any charge being made by the landlord. It is the duty of the landlord moreover to keep his *Jamabandi* upto date, but this he refuses to do unless this

mutation fee is paid and the raiyat pays it because he has a fear at the back of his mind that if he does not pay his title may be questioned, particularly if he wishes subsequently to effect a transfer by sale which can only be done with the landlord's consent. The landlord is therefore charging a fee for keeping his *Jamabandi* upto date, which it is his duty to do without any fee.

10. Under section 84 of the Orissa Tenancy Act all impositions upon a tenant under the denomination of *abwab*, *mathat* or other like appellations, in addition to the actual rent, are illegal, and under section 85 the exaction of such impositions is punishable by fine. I am of opinion therefore that this mutation fee in the case of transfer of occupancy holding by inheritance is an illegal *abwab*, is neither a legal rent nor revenue and is therefore taxable.

11. There is on the file a copy of a letter from the Secretary to the Board of Revenue, Lower Provinces, to the Director of Land Records and Agriculture in Bengal dated the 22nd February, 1893, in which the Board expressed the opinion that the levy of a small fee for registration of transfer or mutations is legitimate. The Board however does not definitely say so, while further this expression of opinion was given 20 years before the Tenancy Act now in force was passed. Finally the Board appears to have arrived at this conclusion because the provisions of the Tenancy Act then in force regarding the registration of mutations do not apply to ordinary raiyati holdings, but it is clear that under section 30 of the Act at present in force an occupancy right is heritable subject to any custom to the contrary. The assessee in this case does not claim that there is any such custom. He cannot therefore interfere with or refuse to recognize a transfer by inheritance and he accordingly cannot charge a fee for recognizing this transfer, which is what he is virtually doing. In other words, he is not in return for this fee giving a consideration which he can legally withhold if the fee is not paid.

12. Assessment in this case has been made on the income of the financial year 1924-25 and on 13th October, 1923, assessee borrowed by taking an overdraft from the Bank the sum of Rs. 501-4-0 for the purpose of buying shares, while on 22nd October, 1924, the assessee borrowed the sum of Rs. 3,030 for the same purpose and Your Lordships have asked me to state a case on the question whether assessee can be allowed as an admissible deduction the amount of interest which he has paid on this overdraft during the "Previous Year". I had noted in my order in review that on a certain date or dates after overdrafts were taken for the purchase of shares, assessee's account with the Bank, if balanced, would have shown a credit balance, and that therefore after that date there was no sum due to the Bank. In this connection I was misled by the claim of the assessee which was not that he should be allowed interest on an overdraft amounting to the total of these two sums referred to above, but interest on a sum of roughly Rs. 9,700, Rs. 6,200 of which was borrowed before July 1923, while the balance of Rs. 3,500 was borrowed partly on 13th October, 1923 and partly on 20th October 1924, and it is true that on 1st October, 1923, there was a credit balance though this was changed to a debit balance by the withdrawal of a cheque for Rs. 3,30,000 on the 2nd October, 1923, for the purpose of purchasing Zemindari, and since that date the balance has invariably been a debit one. Assessee can therefore be allowed interest for the whole of the year 1924-25 on the sum of Rs. 501-4-0, borrowed on 13th October, 1923, while he can be allowed a deduction of interest accrued on the sum of Rs. 3,030 in the period 22nd October 1924 up till the 31st March, 1925. This question would never have arisen if assessee had not made an exorbitant claim and if assessee had been properly represented before me at the time of the hearing of the review.

K. P. Jayaswal and S. M. Gupta, for the Assessee.

Government Advocate and C. M. Agarwala, for the Crown.

JUDGMENT.

COURTNEY TERRELL, C. J.:—This is a reference by the Commissioner of Income-tax under section 66 of the Income-tax Act, 1922. It has been placed before a full Court because the Crown desire to contest the soundness of an earlier decision hereinafter referred to.

The assessee, the Raja of Kanika, derives rather more than one half of his large income from agricultural rents. He has a residential palace upon his estate which extends over about 40 square miles, in which certain quarters are allotted to certain of his Zemindari staff. According to the case stated by the Commissioner "It contains the usual rooms to be found in such a palace including drawing room, dining room, billiard room and bed rooms, while there is a small detached guest house containing one public hall and two bed rooms. The Income-tax Officer in making this assessment has taken Rs. 3,000 as the proportionate valuation of this palace, which is not required for agricultural purposes." The cost of the whole palace was about 4 lakhs of rupees. The proviso to section 2 sub-section (1) (c) of the Act exempts from taxation as agricultural revenue the notional income of a building "which the receiver of the rent or revenue or the cultivator or the receiver of the rent in kind by reason of his connexion with the land, requires as a dwelling-house or as a store house, or other out building." The Department contends that the words "by reason of his connexion with the land requires as a dwelling-house" mean that the proviso is only to apply to such portion, if any, of the building as should be needed as a dwelling house, store house or out building for the purpose of receiving of rents, or cultivation, or receiving of rent in kind as the case may be. The argument more shortly put is that the word "requires" is used in the sense of "needs" and that the words "by reason of his connexion with the land" mean as applied to this case "for the purpose of collecting the rent or revenue."

This interpretation, if correct, would leave the taxable proportion of the notional income from the building to be assessed by the Income-tax Officer as a matter of fact and without appeal. Now I can see no indication in the Act of any circumstances which are to guide the officer in assessing the taxable proportion. There is, for instance, no indication whether the dwelling house is to be of such a kind as to enable the owner to reside in it for such time as may be necessary for the collection by him of his rents, or whether his family may properly be expected to accompany him, or whether the distance from such other dwelling as he may own ought to be considered, or whether his social prestige or the need of displaying it to his tenants is to be taken into account. All these considerations and many others are according to the Department to be left to the officer as matters of fact within his sole discretion. Had this been the real intention of the Legislature one would have expected to find in the Act a set of guiding principles. On the other hand, for assessing the revenue of a business the Act provides elaborate guides. For this reason alone I am of opinion that the Legislature had no such intention as suggested by the Department.

But apart from this consideration the words of the proviso are not capable of the construction suggested. The word "requires" means that the assessee demands to appropriate the building for the purpose of a dwelling house, or as a store house, or other out building and the words "by reason of his connexion with the land" mean that only the fact of his being a receiver of rent or revenue,

or the fact of his being a cultivator, or the fact that he is a receiver of rent in kind entitles him to claim any building as a dwelling house, a store house or an out building. If he should not occupy any of these positions in connection with the land he is not entitled to claim, as tax free, accommodation of the kind specified. In other words, the expression "by reason of his connexion with the land" is merely used to explain the nature of the class of persons entitled to exemption. It has been said that punctuation must not be used in construing a statute other than as a mere *temporanea expositio*, and for this limited purpose it may be noticed that the words are not separated by a comma or otherwise from the words "the receiver of the rent or revenue or the cultivator or the receiver of the rent in kind," whereas the verb "requires" is separated by a comma from the grammatical subject and the phrase "by reason of his connection with the land." My conclusion is that this phrase has a qualitative and not a quantitative significance. Of course there must be a *bona fide* use of the building as a dwelling house, store house or out building and the assessee is not at liberty to claim arbitrarily the exemption of any building which he may at his own choice describe as a dwelling house, store house or out building without regard to the actual facts. For these reasons I am in agreement with the decision arrived at in the case of *Maharajadhiraja of Dhurbanga v. Commissioner of Income-tax*(1).

It has further been argued that the income on account of buildings which is to be exempted from taxation is not the notional income but the actual income, if any, derived therefrom. This argument will hardly bear examination, and I will say no more than that I am in full agreement with the views of my learned brethren on this point.

The next matter for decision is as to whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance is within the definition of agricultural income furnished by the Act, that is to say, "any rent or revenue derived from land which is used for agricultural purposes." It has been contended that the realisation of these mutation fees is illegal and unenforceable. To my mind this is not a circumstance, even if it be the fact, which has any bearing upon the question to be decided. The tenants are admittedly in occupation of agricultural land and however illegal the sum so collected it is paid by the tenant to the landlord by reason of the relationship of landlord and tenant of such land. Such being the case, the mutation fees paid are clearly income derived from land which is used for agricultural purposes and I agree with the former decision above referred to in which the same point was decided in favour of the assessee.

There was a third point as to the admissibility of deductions on account of interest paid on over-drafts but this point does not now call for consideration.

The answers to the questions put by the Commissioner being in favour of the assessee, he should receive 20 gold mohurs by way of costs.

ROSS, J.:—It is conceded that the first question is answered by the decision in *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax*(1), but it is argued that that case was wrongly decided. The learned Government Advocate advanced two alternative arguments.

The first was that this house property is taxable under section 9 and that no section of the Act exempts it from taxation. What is exempted by section 2 clause 1 (c) is income actually derived from a house of the kind therein referred to and as admittedly no income is actually derived from this house there is no exemption. There is more than one answer to this argument. What section 9

taxes is the annual value of buildings, and, where the buildings are in the occupation of the owner, rules are given for ascertaining the annual value to him, which is thus notional income and is taxed as such. But if notional income is taxable, it must also be subject to abatement of tax. Income cannot mean one thing for the purposes of taxation and another for the purposes of abatement. There is therefore no reason for restricting income in section 2 clause 1 (c) to income actually earned. Again, such a construction destroys the meaning of the clause. If a Zemindar lets his house, then he does not require it and therefore it is outside the clause altogether. It is suggested that what the clause refers to is income derived from letting part of the house; but the clause only exempts income from a building owned and occupied by the receiver of rent, and so far as it is not occupied by him, it is not within the exception.

The alternative argument was that advanced by the Commissioner of Income-tax that the house is too large for the assessee's requirements as a Zemindar and is therefore assessable in part. But if the legislature had contemplated such an inquisition into the domestic affairs of the assessee as this argument involves, it seems to me that it would have been expressly provided for. As was observed by Lord Hannen in *Tennant v. Smith*(1), income-tax is imposed not on the personal suitability of the man's surroundings which must vary with the man and the same man in different circumstances, but on his income capable of being calculated. There are three requisites for exemption under this clause: (1) the building must be owned and occupied by the receiver of the rent; (2) it must be on or in the immediate vicinity of the land; and (3) it must be a building which the receiver of the rent by reason of his connection with the land requires as a dwelling house. The first two conditions are admittedly satisfied, and the question is about the third; and this question reduces itself to the meaning of the word 'requires'. In my opinion the meaning is determined by the context and is limited only by the words immediately preceding and following it, namely, "by reason of his connection with the land" and "as a dwelling house." There is no reference, or suggestion of a reference, to the size of the house as a condition of exemption. The only test is that the receiver of rent has to occupy it as a dwelling house by reason of his connection with the land. If by reason of his connection with the land, he has to occupy that house (not a house as large as that), then the notional income derived from the occupation of that house is agricultural income and is exempt from taxation; otherwise the taxability of a Zemindar's house would vary with his zemindary income, the size of his family and his personal tastes. A house free of tax in the hands of one might be taxable in the hands of his successor and a house free of tax at one time might be taxable at another. In my opinion the answer to this argument is that these considerations are outside the Act and that a construction of the section which involves such considerations is not the true construction. I therefore see no reason to alter the opinion expressed in the judgment in *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax*(2), to which I was a party.

On the second question, it is conceded that so far as the mutation fees are fees payable on succession to tenures they are agricultural income; and this is said to be the result of section 14 of the Orissa Tenancy Act which entitles the landlord to a fee in the case of a transfer of a tenure by succession. But it is argued that mutation fees on the transfer of raiyati holdings by succession are not agricultural income because by section 30 of the Act the right of occupancy descends in the same manner as other immovable property in the case of intestacy and any fee taken for mutation of names is an illegal cess. I am unable to see

(1) 3 Tax. Cas., 158.; 1892) A. C. 150.

(2) 3 I. T. C. 158.

how the legality or illegality of a charge affects the source from which the income is derived. If a mutation fee on the transfer of a tenure is agricultural income, it is difficult to see on what principle the mutation fee on the transfer of a raiyati holding is not agricultural income also. In my opinion both these payments are equally revenue issuing from the land or, what is the same thing, from the relation of landlord and tenant.

Learned Counsel for the assessee pressed for a decision on the question of the legality of these charges. It is contended that section 30 merely states the rule of devolution of occupancy holdings in the case of intestacy and that the exaction of a mutation fee would be governed by custom, at any rate in a permanently settled estate. It is said that this custom has been recognized in the instructions of the Board of Revenue in 1893, and that it is followed by the Government itself as proprietor of the Khurda estate. This may be so, but the question seems to me to be altogether outside the jurisdiction of the Commissioner of Income-tax; and, consequently, not fit for decision by this Court in the present proceeding.

WORT, J.:—This is a case stated by the Commissioner of Income-tax under an order of this Court, dated the 22nd November, 1927. The Court required the Commissioner to state a case on three matters. As regards the third, however, the attitude adopted by the Commissioner before the order of the 22nd November 1927, appears to have been under a misapprehension of the facts and it has now been adjusted and the Crown concedes that the assessee is entitled to the deductions which were claimed in regard to this.

The remaining questions are two in number. The first is whether the house occupied by the assessee on his estate at Karika is entitled to complete exemption as agricultural income under the provisions of section 2 sub-section (1) (c) and section 4 (3) (viii) of the Income-tax Act.

The second question that arises is whether certain mutation fees which are a part of the Zemindar's income are agricultural income within the meaning of section 2 sub-section (1) (a) of the Act.

It will be necessary in dealing with these points to state briefly the facts. The Raja of Kanika has a palace at Kanika which appears to have cost something like three lakhs of rupees apart from the zenana quarters. This palace is situated on his zemindari which is of an area of 439 square miles.

In the case stated it is admitted that the description of the palace complies with section 2 sub-section (1) (c) in that it is on or in the immediate vicinity of the land and that the building is owned and occupied by the assessee being the receiver of the rents and profits. The question which the Commissioner of Income-tax states arises is whether the whole valuation, that is, the annual value of the residence of this Zemindar should be exempted from income-tax regardless of the proportion between that valuation and his income from landed property and regardless further of the proportion which his income from landed property bears to his income from other sources. The Commissioner further states in the case that the assessee's income from rent proper is approximately 50 per cent. of his total income. Further he states that it is submitted that this palatial building is not required wholly and exclusively for agricultural purposes and that the question of valuation of what proportion of the total building the assessee should be assessed at is a question of fact in each case. The amount of the assessment of the building or a part thereof is undoubtedly a question of fact but nowhere in the Act does it provide that the dwelling house should be required for agricultural purposes. The Act uses the expressions "required as a dwelling house in connexion with the land."

The second section defines "agricultural income" and sub-section (1) (c) includes any income derived from any building owned and occupied by the receiver of rent or revenue of any such land, and eliminating irrelevant portions it goes on to provide that the building is on or in the immediate vicinity of the land and is a building which the receiver of the rent or revenue by reason of his connection with the land requires as a dwelling house, etc.

The question which arises is a question of mixed fact and law. But the real point before us, having regard to the findings of fact by the Commissioner, is what is the proper construction to be placed upon the words "required as a dwelling house in connection with the land."

The question has already come up before this Court and it has been decided in the case of *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax, Bihar and Orissa*(1), that it is sufficient to show that by reason of the assessee's connexion with the land he requires a dwelling house in the vicinity and that it is not open to the Commissioner to consider whether the particular class of house is more or less the actual requirements of the Zemindar. One of the questions really before us is whether that case was rightly decided.

I have already indicated the view which the Commissioner takes with regard to the meaning of these words, and, in my judgment, clearly the test which he applies is a fallacious one.

It is important to notice that there is a statement by the Commissioner that the Income-tax Officer in making this assessment has taken Rs. 3,000 as the proportionate valuation of the portion of this palace which is not required for agricultural purposes. I would be content in founding my judgment on this statement or the inference to be drawn from it, having regard to the other facts which have been found in the case. This last statement, in my judgment, is tantamount to saying that the Raja requires this palace as a dwelling house in connection with the land, or to put it in other words, that having found that a portion of the building on the land is required for the purposes set out in the Act, the section has been complied with and that a Court is thereafter precluded from any further inquiry and that there is nothing in the Act to warrant his inquiring into what portion of the building is so required.

I have already stated that the Commissioner adds the words "required for agricultural purposes"; but there is no justification for these words "agricultural purposes" whatever. Equally there is no justification for the method which the Commissioner has adopted, namely, of testing the question by determining the proportion between "agricultural income" of the Zemindar to that of his total income.

However, as the question is really one as to the true construction of the Act, I propose to deal with the arguments which have been advanced with regard to it.

The first argument put forward by the learned Government Advocate on the construction of section 2 is one which is diametrically opposed to the contentions of the Income-tax Department, but that is immaterial, the contention being that when the word "income" is used in section 2 sub-section (1) (c) the meaning is actual income and not notional income: that is, income must mean actual money received as a profit from the building.

It is further contended in support of this argument that there is only one section in the Act which deals with notional income and that is section 9.

It is obvious that the Crown must be driven back as it was to the contention that the exception under section 2 was not an exception to section 9.

For the purposes of this argument the Crown relies upon the case of *Tennant v. Smith*(1). The judgment in that case however gives no support to this argument. The judgment which related to the assessment of a bank manager under Schedule D of the Income-tax Act in England then in force, that is to say, the Act of 1842 and the question therein arising was whether the occupation of a house provided for him by his employees was an emolument within the meaning of that Schedule. The words in that judgment relied upon by the Crown are those in Lord Halsbury's speech "that the thing sought to be taxed is not income unless it can be turned into money."

The case as I have stated dealt with words quite different from those we have to construe. In effect the argument is this: that wherever the word "income" is used it means actual money or money's worth and not notional income in the sense of an annual value of a house occupied by the assessee. One answer to that argument is that the Income-tax Act as its name denotes deals with the taxation of income under several heads and one is "property" [Section 6 (iii)]. That so far as property is concerned notional income is taken. In other words section 9 (1) provides that the assessee in regard to Property shall be taxed on the *bona fide* annual value.

I think that statement is sufficient to meet the argument that actual income only is dealt with by the Act. The Crown in the case stated recognises this to be a case of notional income but says that it is an exception to the general meaning of the word income. But the plain construction of section 2 is a complete answer to the argument. The Act must be construed so as to give it a reasonable meaning. The effect of the construction contended for would be to repeal the provisions of section 2, or to make them a nullity. The dwelling house to be exempt must be owned and occupied by the receiver of the rents and profits of the agricultural land, and it must be required as a dwelling house. If it is occupied how can actual cash income accrue from it and indeed if it is occupied by a third person who will pay rent and thus render income to the owner, how can it be said that it is required as a dwelling house by the owner assessee. In my judgment this is an impossible construction.

The main argument however is that there must be some sort of relation or rather proportion to be fixed as between the dwelling house and the land or Zemindari and that is always a question of fact for the Commissioner. The words to be construed, therefore, are (substituting the phrases used so far as their positions in the section are concerned) "required as a dwelling house in connexion with the land". Now it is not argued that the Commissioner would be required, nor is he required, to enquire into the actual reasonableness of the demands of the Raja so far as the dwelling house is concerned. That is to say, he may live in any style he likes and have a palace or a hut. But it is said that the words "in connexion with the land" place limits upon or condition the Raja's requirements with regard to a dwelling house so far as the exemption from taxation is concerned. Do these words warrant any such argument? The Crown contends that the words warrant the following enquiries which the case stated suggests:—(i) Whether the assessee occupies the house *qua* landlord; (ii) What proportion does his income from land bear to his income from other sources; (iii) Whether the palace is required exclusively for agricultural purposes. The Crown contends as to (1) that the assessee does not occupy the house *qua* landlord. Then in what capacity does he occupy? In my judgment

in as much as he is entitled to a partial exemption according to the case stated he does in fact occupy the house *qua* landlord. That is to say that this or that part of the palace is not required by his occupation *qua* landlord or for agricultural purpose is either enquiring into the assessee's personal habits or tastes, an enquiry quite irrelevant on any construction to be placed upon the section, or to apply a test which the language of the Act in no way warrants. The section says requires as a dwelling house in connexion with the land, not requires as a dwelling house in connexion with and for the purposes of the land (or agriculture). If we were to read "for the purposes of agriculture" into the section which in effect the argument of the Crown contends for, the whole house would be outside the provisions of the section. Neither the dining room nor any of the living rooms are required in connexion with the land any more than the billiard room or zenanna quarters, placing the construction desired by the Crown upon the section.

In my judgment if the argument on behalf of the Crown is right then the construction contended for in the case stated is the only tenable one, that is, that only "Zamindari Kacherries, Manager's Offices and buildings of that nature" are exempt, and that contention is clearly wrong on any plain reading of the section, the sub-section stating as it does that dwelling house, or store house or other out buildings are exempt.

In my opinion the words we have to construe "in connexion with the land" merely make it necessary for the assessee to establish the relation between himself and his house with the land in order to claim exemption. Such relation in this case is established as a fact and in my judgment any further enquiry is precluded. The hypothetical case of a person building a palace on a few bighas of land with, say, one small holding seems hardly to touch the point. First such a case in India is unlikely to occur and secondly the case is so extreme that neither as a question of law or fact could it be stated that such a house was required as a dwelling house in connexion with the land: on the other hand the land would be required in connexion with the house or as one of its amenities, an exemption for which the statute does not provide. I would therefore hold that the case of *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax*(1), was rightly decided on this point and should be followed. In addition I think there can be no doubt that but for the exception contained in the sub-section under discussion, this palace would be taxable under section 9 as property. The assessee could not be heard to say that not all the palace was occupied by him and therefore not all of it should be taxed. The same construction should be placed upon the words under consideration whether they in fact involve exemption or taxation.

I see nothing in the Act to justify the argument that being required as a dwelling house yet only a portion is to be exempt.

The next point relates to the mutation fees. Sir Sultan Ahmad on behalf of the Crown admits that the basis of the Commissioner's contention so far as the fees secured by the Raja on the transfer of tenure was wrong and that the assessee is entitled to treat these as agricultural income within the meaning of the Act and therefore exempt. However his admission, as I understand it, goes only so far as the case in which the amount chargeable by the Raja is one which he is entitled by law to recover and not so far as any excess amount is concerned.

The other mutation fees are those realised from occupancy ryots and it is contended that as these are illegal *abwabs*, they can in no sense be termed revenue from land within the meaning of section 2 sub-section (1) (a).

In dealing with this latter point therefore I shall deal with that portion of the mutation fee on the transfer of tenures which is stated by the Crown to be illegal.

In the first place it was argued that the test which was to be applied in order to discover whether mutation fees could be treated as "agricultural income" within the meaning of the section, depended upon the question whether these fees were enforceable or not and this argument was supported by the case of *King Emperor v. Probhat Chandra Barua*(1), where it was decided that fees on petitions payable with regard to transferable holdings (as these were) were not "agricultural income." With this case I shall deal presently, but whether this authority decides that the legality of the fees is the real test, in my judgment it is impossible to say that the character of the fee is altered by the fact that it is irrecoverable; rent may be irrecoverable by reason of the fact that it is higher than the amount reserved in a lease, or that in an occupancy holding, an enhancement not allowed by the statute law is claimed. But the real character of both still remains, that of rent, and to repeat, to say that a thing is changed in character by reason of its being irrecoverable is beside the point.

It is contended by the respondent that mutation fees in respect of occupancy holdings were recoverable by means of a custom which existed for many generations past. But in the view that I take of the matter whether they are recoverable or irrecoverable is irrelevant in coming to a conclusion whether these fees are "agricultural income" and therefore that question had not been decided. The case which I have quoted and upon which the learned Government Advocate relies mentions the authority of *Meher Bano Khanum v. Secretary of State for India*(2), and the learned Judges deciding that case have differentiated the case of *Birendra Keshore v. Sec. of State*(3), on the ground that what the learned Judges were referring to was *nazar* which was paid by a tenant for the recognition of a transfer of a non-transferable occupancy holding and that in effect *salami* or *nazar* paid in those circumstances really amounted to the capitalised value of a part of the rent for a new settlement. In my judgment, quite clearly, if that was the basis of the decision in the case of *Meher Bano Khanum v. Secretary of State for India*(2), then what the Court was there deciding was that *nazar* was rent, for the reason that capitalised rent is rent.

The question which we have to determine is whether these fees are rent or revenue within the meaning of section 2 sub-section (1) (c) and these fees do not cease to be revenue by reason of the fact that *nazar* was capitalised rent. These fees are not rent.

One of the questions, therefore, for determination is whether the Legislature in using the expression "rent" or "revenue" intended by the word "revenue" something other than "rent". In my opinion the word "revenue" is not to be construed as *ejusdem generis* with rent. "Rent" has characteristics which are well known to lawyers. "Revenue" whilst it may be a species of agricultural income has, in my judgment, a wider meaning than rent.

Now from what source do these fees come? Is it by reason of the relation that the person recovering them has with the land? I think this question

(1) 2 I.T.C. 392.

(2) 2 I.T.C. 99.

(3) 1 I.T.C. 67.

must obviously be answered in the affirmative; and apart from the fact that they may not be recoverable in law, I do not see any distinction, between *nazar* and or *sāmi* in the case of a tenure and the fee paid with regard to occupancy holdings. If the former is "revenue", I do not see how it can be argued that the other is not revenue as well. In this connection it is important to notice again that what the case of *King Emperor v. Probhat Chandra Barua*(1), has decided is that *nazar* was revenue although the reason which is given in the case of *Meher Bano Khanum v. Secretary of State for India*(2), for that decision is that *nazar* was in the nature of rent. It is not suggested before us that the fees in this case are rent, but it is argued it is not revenue. If that is the *ratio decidendi* of the case of *Meher Bano Khanum v. Secretary of State for India*(2), then it would appear to be of no assistance to us in determining the question of whether these fees are revenue within the meaning of section 2.

The Oxford Dictionary definition of the word "revenue" has been referred to in the case stated but I see no support for the Crown's argument from that definition; the definition is a return, yield, or profit of any land, property or other sources of income. Can it be doubted for a moment that this is a return or yield or profit from property or landed property? It is undoubted that but for the ownership of this land, this source of income, using that word in a neutral sense would not be available to the assessee. I would hold, therefore this is agricultural income in the sense that it is revenue from land.

In my judgment, all the points which are before us should be answered in favour of the assessee, that is to say, that on the facts proved or admitted the whole of the palace at Kanika should be exempt under section 2. The fees on the transfer of tenures and the fees for the mutation of names with regard to occupancy holdings are agricultural income within the meaning of the section referred to.

KULWANT SAHAY, J.:—The questions which arise for determination in this reference under section 66 of the Income-tax Act are:—(1) whether any portion of the valuation of the assessee's palace at Kanika is taxable, or, whether on the other hand, the whole valuation of this palace should be exempted as being agricultural income within the meaning of section 2 (1) (c) of the Act; (2) whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance are covered by the term "agricultural income" as defined in section 2 of the Act and (3) whether the assessee can be allowed as an admissible deduction the amount of interest which he has paid on overdrafts during the "previous year."

As regards the first point: section 4 (3) sets out the classes of income to which the Act shall not apply, and one of these classes is agricultural income. "Agricultural income" is defined in section 2 (1) of the Act. Section 2 (1) (c) makes income derived from any building owned and occupied by the receiver of the rent or revenue of any such land, or occupied by the cultivator, or the receiver of rent-in-kind, of any land with respect to which, or the produce of which, any process mentioned in sub-clauses (ii) and (iii) of clause (b) is carried on. To this there is a proviso to the effect that the building is on or in the immediate vicinity of the land and is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land, requires as a dwelling house, or as a store-house, or other out-building. The question is whether the assessee can rely upon this proviso for exemption of his house from taxation. Section 6 of the Act gives the heads of income, profits and gains which shall be chargeable to income-tax in the manner

provided in the Act, and one of these heads is "property." The manner in which 'property' is chargeable to income-tax is given in section 9, sub-section (1) of which provides that the tax shall be payable by an assessee under the head "property" in respect of the *bona fide* annual value of the property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of his business, subject to certain allowances set out in the section. In the case of buildings in the occupation of the owner it is the notional income upon which the tax is to be payable. It is contended on behalf of the Crown that the house in question in the present case is taxable under section 9, and that what is exempted by section 2 (1) (c) is income actually derived from any building owned and occupied by the receiver of the rent or revenue and does not include the notional income of the building. In my opinion this contention is unsound and cannot be accepted. Section 2 (1) of the Act gives the definition of "agricultural income," and chapter III, deals with taxable income; section 6 gives the heads of income and section 9 provides for the mode of determining the income taxable under the Act under the head "property." Such income under section 9 in respect of buildings in the occupation of the owner must be notional income, and the argument of the learned Government Advocate that what is exempted by section 2 (1) (c) is actual income is contrary to the provisions of the Act itself.

The real question, however, for determination is what is the meaning of the proviso to section 2 (1) (c). In order that the income derived from any building may be held to be agricultural income, it is necessary that the building must be (1) on or in the immediate vicinity of the land and (2) it is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land requires as a dwelling house or as a store-house or other out-house or other out-building. It is conceded in the present case that the building in question is on or in the immediate vicinity of the land. It has been found by the Commissioner as a fact that a part at least of the building is required by the receiver of the rent or revenue as a dwelling house, by reason of his connection with the land. The question is whether there is any justification in the Act for the Commissioner to decide what portion of the building the assessee does in fact require as a dwelling-house by reason of his connection with the land. In my opinion, the moment it is found that the building or any portion of it is required by the receiver as a dwelling house the income derived from such building would become agricultural income and exempt from taxation. The argument that the word "requires" gives the Income-tax authorities the power to determine what portion of the building is as a matter of fact required by the assessee in his capacity of receiver of the rent is, in my opinion, not warranted by the terms of the section. I agree with the reasons given by my Lord the Chief Justice and by Ross and Wort, JJ., for holding that the construction sought to be placed upon the proviso by the Income-tax authorities is not warranted by the terms of the section. It would no doubt be open to the Income-tax authorities to hold that a particular building on account of its size or situation is not a building which the receiver of rent or revenue does require, by reason of his connection with the land, as a dwelling house and in that case it would be open to them to assess the income from the entire building, but the moment they find that the house is required by the receiver of the rent or revenue by reason of his connection with the land as a dwelling house or a store-house or other out-building, it is beyond their jurisdiction to determine what portion of the building is or should be required by the assessee as such receiver of the rent or revenue. In my opinion the case of *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax*(1), was

correctly decided and I would answer the first part of the first question in the negative and the second part in the affirmative.

As regard the second point: I agree for the reasons given by my Lord the Chief Justice and by Ross and Wort, JJ., that mutation fees paid by tenants upon succeeding to holdings or tenures are covered by the term "agricultural income" as defined in section 2 of the Act. The question whether such fees are legally recoverable or not is a question beyond the jurisdiction of the Income-tax authorities. The words "rent or revenue derived from land which is used for agricultural purposes" in section 2 (1) (c) of the Act are wide enough to cover receipts by landlords in the shape of mutation fees.

As regard the third point: the learned Commissioner finds that the assessee is entitled to claim deduction of the amount of interest which he has paid on overdrafts during the previous years and the question does not arise for determination.

MACPHERSON, J.:—Under section 66 of the Indian Income-tax Act, 1922 the Commissioner of Income-tax has, as required by this Court in its order of the 22nd November, 1927, stated a case on three questions and referred the same to this Court with his own opinion thereon. The assessee is the proprietor of the Kanika estate in Orissa.

The first question is whether any portion of the valuation of the assessee's palace at Raj-Kanika is taxable, or whether on the other hand the whole valuation on this palace should be exempted as being agricultural income within the meaning of section 2 (1) (c) of the Act. The facts are briefly these. The gross income of the assessee comes to Rs. 3,90,000, of which income from agricultural rent is approximately Rs. 2,10,000. The Manager's office which also houses the Zemindari staff is a separate and older building. In the palace proper only seven of the Zemindari staff are accommodated and practically the whole of the building is used as a residence for the assessee and for visitors. It was built in 1912 at a cost of Rs. 3,00,000 and zenana quarters were subsequently added at a cost of Rs. 1,00,000. It has the ordinary accommodation of a palace and there is a detached guest-house. The Commissioner states: "The Income-tax Officer in making the assessment has taken Rs. 3,000 as the proportionate valuation of the portion of the palace which is not required for agricultural purposes." It would appear that the expression "requires for agricultural purposes" here means "which the assessee by reason of his connection with the land requires as a dwelling house."

The Commissioner sets out that it is the contention of his department that the palace is not occupied by the receiver of rent, nor required by him *qua* landlord as a dwelling house, store-house or other out-building. The assessee's income from rent proper is approximately fifty per cent. of his total income and it is contended that "the assessee requires or has built his palatial residence not because he requires such a building by reason of his connection with the land but because his total income and high social position demand." The Commissioner submits that "this palatial building is not required wholly and exclusively for agricultural purposes and that the question of the valuation of what proportion of the total building assessee should be assessed is a question of fact to be decided in each case," regard being had in coming to a decision to the provisions of the proviso to section 2 (1) (c) of the Act and in particular to the point whether the building in question or the whole of the building is required (as dwelling house) by reason of the assessee's connection with the land. The assessee, he repeats, has been taxed only on a small portion of the annual valuation of the palace proper.

The short point therefore is whether the palace proper is a building which the assessee (who is admittedly the receiver of the rent or revenue derived from the land of Kanika estate which is used for agricultural purposes and which is assessed to land-revenue in British India) by reason of his connection with the land requires as a dwelling house. If it is such a building, the annual value of it is agricultural income and the Act does not apply to it as admittedly it is on the land; if it is not such a building, the Act applies.

Now the proviso to section 2 (1) (c) limits the building owned and occupied by the assessee the valuation of which is agricultural income under the definition, to a building of the class described in the proviso—it must be one which the receiver of the rent or revenue of the land by reason of his connection with the land requires as a dwelling house. The submission on behalf of the assessee is practically that this proviso is satisfied if the building is one *which or a part of which* the receiver of the rent or revenue of the land by reason of his connection with the land *uses* (or even states that he uses) as a dwelling house. But such does not appear to be the intention. It is indeed not even arguable that mere use or allegation of use or even allegation of need satisfies the proviso. It is sufficient therefore to discuss the case where the building is one a part only of which the assessee by reason of his connection with the land *requires* as a dwelling house where the word 'requires' is taken as equivalent to 'needs'. Now if the Legislature had contemplated that the assessee's requirement by reason of his connection with the land of a part merely of the building as a dwelling house would be sufficient, what prevented it from saying that? The connotation of the expression "by reason of his connection with the land requires" must be "needs as appropriate and convenient for his calling as a receiver of the rent or revenue derived from the land." The learned Counsel for the assessee would practically read the proviso (so far as is material) as "Provided that.....the receiver of the rent or revenue.....by reason of his connection with the land requires a dwelling house." But the enactment contemplates that he must by reason of his connection with the land require the particular building as a dwelling house. In this Province the case of the great Indigo concerns of North Bihar readily occurs to one. The residence of the owner or manager was appropriate to the extensive landed interests of the Concern. But it is otherwise when on the dissolution of the Concern that building is acquired with some neighbouring land constituting but a small fraction of the territory of the Concern and is occupied by the purchaser mainly not by reason of his connection with the adjoining land but for merely residential reasons, or from considerations of local prestige, or for sporting purposes, or some similar object. The Legislature cannot have intended to exempt such purchasers from income-tax on the building. To my mind language has been employed which indicates an intention to discriminate between the requirements of the assessee as the landlord and his requirements as an individual. In the present instance it is found as a fact that the whole palace is not a building which the assessee as receiver of the rent or revenue of the land "by reason of his connection with the land requires as a dwelling house," and accordingly it is not such a building as is described in section 2 (1) (c) read with the proviso and therefore the notional income thereof is not agricultural income so as to be under section 4 (3) (viii) outside the application of the Act. Strictly therefore the whole palace falls within section 9 and it was apparently open to the Commissioner to assess the notional income from it accordingly. No doubt the Income-tax department has further found that a portion of the palace comes within the proviso and it has not assessed the income from such portion to income-tax. But we are not concerned here with the attitude of the department in taking what may be less than its full right, except to this extent that if, as is contended (in my opinion erroneously) the total annual value of the whole palace and not the proportionate value of the portion not required as a dwelling house by the receiver of the

rent or revenue of the land, is Rs. 3,000, the assessment would still not be illegal. It is however sufficient in the present reference to answer the first portion of the question in the affirmative and the second portion in the negative. In my opinion the reference in *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax, Bihar and Orissa* (1), was not correctly decided.

The second question is whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance come within the definition of 'agricultural income' as defined in the Act, so that the Act does not apply to them. As admittedly the land is assessed to land-revenue in British India, the point shortly is whether these fees come within the expression "any rent or revenue derived from land which is used for agricultural purposes." The tenants referred to are of two classes: (1) tenure-holders, and (2) raiyats.

A tenure-holder pays the fee under section 14 of the Orissa Tenancy Act. The Commissioner points out that the fee is not within the definition of 'rent' under that Act and indicates that if the expression 'revenue' is to be taken in so wide a sense 'agricultural income' would include illegal realisations, such as *abwabs*. This however does not appear to be the correct criterion, since 'rent' in the Tenancy Act has by definition a restricted meaning appropriate to such an enactment but inappropriate to an Income-tax Act, and the learned Government Advocate is unable to contend that the fee paid by a tenure-holder to the landlord under the statute is not "rent or revenue derived from the land" and therefore "agricultural income."

As to the succession fees paid by the raiyats in this permanently settled estate, the Commissioner considers that they are illegal impositions under section 84 of the Orissa Tenancy Act, the exaction of which is punishable by fine under section 83. In short "the landlord is charging a fee for keeping his jamabandi up to date, which it is his duty to do without any fee", and the payment is therefore one without consideration.

Here again the chief fallacy appears to lie in the Commissioner's assumption that the expression 'rent' in the Income-tax Act, 1922, has the same meaning as it has in the Orissa Tenancy Act. Payments to the landlord which are not 'rent' under the Tenancy Act which term is as usual in such enactments defined for the purpose of the Act as "whatever is *lawfully* payable.....", may well be 'rent' derived from the land within the meaning of the Income-tax Act, where not the legality or morality but the character and origin of the income are in point.

It has been urged, not very convincingly perhaps, that the payment is even 'rent' within the meaning of the term in the Tenancy Act but it is not necessary to determine the point. The small fee legally or illegally paid by a raiyat to his landlord for the mutation in the landlord's papers of his name by virtue of succession appears not to be a mere payment for a service but to fall within the wide expression "rent or revenue derived from the land," irrespective of any dissection of the individual terms 'rent' and 'revenue'. I would answer the question in the affirmative.

The third point is whether the assessee can be allowed as an admissible deduction the amount of interest which he has paid on certain overdrafts during the 'previous year.' The Commissioner points out that the assessee can be allowed interest for 1924-25 on Rs. 501-4-0, borrowed on the 13th October, 1923, and a deduction of interest which accrued on Rs. 3,030 in the period 22nd October 1924 to 31st March 1925. There is no controversy on this point and I would answer it in the affirmative.

in making this assessment has taken 3,000 as the proportionate valuation of the portion of this palace, which is not required for agricultural purposes.

4. As required I state my opinion on the questions of law raised.

5. If the valuation of the building in question is to be exempted, the following conditions must be fulfilled: (1) it must be owned and occupied by the receiver of rent or revenue from agricultural land, (2) the building must be on or in the immediate vicinity of the agricultural land, and (3) it must be a building which the receiver of the rent or revenue by reason of his connection with the land requires as a dwelling house or store house or other out building. It is admitted that the palace in question is on or in the immediate vicinity of the land, the rent of which the assessee receives, and it is not denied that this building is owned and occupied by the assessee, who is a receiver of rent, but it is the contention of the Department that it is not occupied by him *qua* receiver of rent and that it is not required by him *qua* landlord as a dwelling house, store house, or other out building. The real point at issue is whether the valuation of the whole of the residence of a Zemindar should be exempted from income-tax, regardless of the proportion between that valuation and his income from landed property and regardless further of the proportion which his income from landed property bears to his income from other sources. In this case, assessee's income from rent proper is approximately 50 per cent of his total income and in my view assessee requires or has built this palatial residence not because he requires such a building by reason of his connection with the land but because his total income and high social position demand it. It would, in my view, be straining the law unfairly to hold that the total value of this building is exempt from income-tax by reason of the provision of section 2 (1) (c) of the Act, read with section 4 (3) (viii) and section 2 (1) (c) should be interpreted as giving exemption only to Zemindari Katcheries, Manager's offices and buildings of that nature. It is submitted therefore that this palatial building is not required wholly and exclusively for agricultural purposes and that the question of the valuation of what proportion of the total building assessee should be assessed is a question of fact to be decided in each case, regard being had in coming to a decision to the provisions of the proviso to section 2 (1) (c) of the Act and in particular to the point whether the building in question or the whole of the building is required by reason of the assessee's connection with the land. In this case assessee has not been taxed on the valuation of the out buildings or Zemindari Office, but only on a small proportion of the annual valuation of the palace proper.

6. The next question on which your Lordships have asked me to state a case is "Whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance are covered by the term "Agricultural income" as defined in section 2 of the Income-tax Act of 1922".

7. The term 'tenant' includes both tenure holders and raiyats and under section 14 of the Orissa Tenancy Act (Act 2 of 1913), the landlord is bound to recognize the transfer of a tenure by succession, only provided the transferee pays him a fee amounting to Rs. 2 except in the case of a *Baji aftidar* when the fee shall be Re. 1, while under section 30 of the Act, if a raiyat dies intestate in respect of a right of occupancy it shall, subject to any custom to the contrary, descend in the same manner as other immovable property. In my order in review, when dealing with this point I held that mutation fees realized from occupancy raiyats was an illegal *Abwab* and therefore taxable, while the question whether fees realized on the occasion of transfer of tenures is taxable or not would depend on the finding of Your Lordships in a case already before you and as there was no evidence on record which would enable me to separate the taxable portion of the amount of income shown under this head by the assessee in the explanation

attached to his return of income, viz., Rs. 4,466 from the portion which may not be taxable I refused to interfere with the order of assessment taxing the whole sum as originally shown in the explanation attached to the assessee's return of income.

8. I deal first with the question whether mutation fees paid by tenure holders on succession by inheritance are covered by the term "Agricultural income" as defined in section 2 of the Income-tax Act, 1922. As stated above, under section 14 of the Orissa Tenancy Act of 1913, the landlord is bound to recognise the transfer of a tenure by succession only provided that the transferee pays him a fee amounting to Rs. 2 in certain cases and Re. 1 in others. Assessee's representative alleges that though under the law assessee can realize this amount he as a matter of fact realizes only at the same rates as in the case of transfer of occupancy rights by succession, namely, at the rate of annas two per acre with a minimum fee of annas four and a maximum fee of Re. 1. This transfer fee is not covered by the term "Rent" as defined in section 2 sub-section 1C of the Orissa Tenancy Act and the question is whether it is revenue derived from land which is used for agricultural purposes and the answer to this question would appear to depend on the correct definition of the word "Revenue". This word has been defined in the Oxford Dictionary as, "the return, yield or profit of any land, property or other important source of income; that which comes into one as a return from property or possessions, specially of an extensive kind; income from any source specially of an extensive kind; income from any source but specially when large and not directly earned". If it is held that landlord's fees is money which comes to the landlord by virtue of the fact that he is the owner of the land it is agricultural income, but if this view is correct and the word revenue is taken in this wide sense the result would be to include within the meaning of agricultural income illegal realisations or *Abwabs*, which a landlord realised by virtue of his position as a landlord though these are neither agricultural rent nor revenue. In my opinion the correct way to view these receipts is to hold that they are not rent or revenue derived from land, but are payable by a tenure holder under a liability incidental to the ownership of the tenure.

9. According to the statement of assessee's representative the rate charged is two annas per acre with a minimum fee of four annas and a maximum fee of Re. 1. In the case of each application for transfer regular printed forms are used and a regular file is opened. No raiyat has so far refused to pay this fee—at least not to the knowledge of assessee's representative who appeared before me and has been serving the Estate for twelve years, but on the other hand if a successor by inheritance refuses to pay this fee, the Estate would refuse to recognize him and when he came to pay rent for the holding the receipt would be issued in the name of the deceased occupant, through the payer. In other words, unless this fee is paid the landlord refused to recognize the new raiyat and refused to keep his *Jamabandi* upto date. Assessee's representative does not advance the claim that an occupancy holding is not heritable except with the consent of the landlord. He refused to commit himself on the question whether he could claim this mutation fee in law and on the further question whether steps would be taken to dispossess the succeeding raiyat if he failed to pay the mutation fee; he alleged that if the inheritor does not pay the mutation fee the assessee would refuse to recognize him though he is a tenant in the eye of the law. The position then is this. Occupancy rights are heritable, subject to any custom to the contrary. No such custom has been claimed in the case of this estate and therefore occupancy right should pass to the successor without any charge being made by the landlord. It is the duty of the landlord moreover to keep his *Jamabandi* upto date, but this he refuses to do unless this

mutation fee is paid and the raiyat pays it because he has a fear at the back of his mind that if he does not pay his title may be questioned, particularly if he wishes subsequently to effect a transfer by sale which can only be done with the landlord's consent. The landlord is therefore charging a fee for keeping his *Jamabandi* upto date, which it is his duty to do without any fee.

10. Under section 84 of the Orissa Tenancy Act all impositions upon a tenant under the denomination of *abwab*, *mathat* or other like appellations, in addition to the actual rent, are illegal, and under section 85 the exaction of such impositions is punishable by fine. I am of opinion therefore that this mutation fee in the case of transfer of occupancy holding by inheritance is an illegal *abwab*, is neither a legal rent nor revenue and is therefore taxable.

11. There is on the file a copy of a letter from the Secretary to the Board of Revenue, Lower Provinces, to the Director of Land Records and Agriculture in Bengal dated the 22nd February, 1893, in which the Board expressed the opinion that the levy of a small fee for registration of transfer or mutations is legitimate. The Board however does not definitely say so, while further this expression of opinion was given 20 years before the Tenancy Act now in force was passed. Finally the Board appears to have arrived at this conclusion because the provisions of the Tenancy Act then in force regarding the registration of mutations do not apply to ordinary raiyati holdings, but it is clear that under section 30 of the Act at present in force an occupancy right is heritable subject to any custom to the contrary. The assessee in this case does not claim that there is any such custom. He cannot therefore interfere with or refuse to recognize a transfer by inheritance and he accordingly cannot charge a fee for recognizing this transfer, which is what he is virtually doing. In other words, he is not in return for this fee giving a consideration which he can legally withhold if the fee is not paid.

12. Assessment in this case has been made on the income of the financial year 1924-25 and on 13th October, 1923, assessee borrowed by taking an overdraft from the Bank the sum of Rs. 501-4-0 for the purpose of buying shares, while on 22nd October, 1924, the assessee borrowed the sum of Rs. 3,030 for the same purpose and Your Lordships have asked me to state a case on the question whether assessee can be allowed as an admissible deduction the amount of interest which he has paid on this overdraft during the "Previous Year". I had noted in my order in review that on a certain date or dates after overdrafts were taken for the purchase of shares, assessee's account with the Bank, if balanced, would have shown a credit balance, and that therefore after that date there was no sum due to the Bank. In this connection I was misled by the claim of the assessee which was not that he should be allowed interest on an overdraft amounting to the total of these two sums referred to above, but interest on a sum of roughly Rs. 9,700, Rs. 6,200 of which was borrowed before July 1923, while the balance of Rs. 3,500 was borrowed partly on 13th October, 1923 and partly on 20th October 1924, and it is true that on 1st October, 1923, there was a credit balance though this was changed to a debit balance by the withdrawal of a cheque for Rs. 3,30,000 on the 2nd October, 1923, for the purpose of purchasing Zemindari, and since that date the balance has invariably been a debit one. Assessee can therefore be allowed interest for the whole of the year 1924-25 on the sum of Rs. 501-4-0, borrowed on 13th October, 1923, while he can be allowed a deduction of interest accrued on the sum of Rs. 3,030 in the period 22nd October 1924 up till the 31st March, 1925. This question would never have arisen if assessee had not made an exorbitant claim and if assessee had been properly represented before me at the time of the hearing of the review.

K. P. Jayaswal and S. M. Gupta, for the Assessee.

Government Advocate and C. M. Agarwala, for the Crown.

JUDGMENT.

COURTNEY TERRELL, C. J.:—This is a reference by the Commissioner of Income-tax under section 66 of the Income-tax Act, 1922. It has been placed before a full Court because the Crown desire to contest the soundness of an earlier decision hereinafter referred to.

The assessee, the Raja of Kanika, derives rather more than one half of his large income from agricultural rents. He has a residential palace upon his estate which extends over about 40 square miles, in which certain quarters are allotted to certain of his Zemindari staff. According to the case stated by the Commissioner "It contains the usual rooms to be found in such a palace including drawing room, dining room, billiard room and bed rooms, while there is a small detached guest house containing one public hall and two bed rooms. The Income-tax Officer in making this assessment has taken Rs. 3,000 as the proportionate valuation of this palace, which is not required for agricultural purposes." The cost of the whole palace was about 4 lakhs of rupees. The proviso to section 2 sub-section (1) (c) of the Act exempts from taxation as agricultural revenue the notional income of a building "which the receiver of the rent or revenue or the cultivator or the receiver of the rent in kind by reason of his connexion with the land, requires as a dwelling-house or as a store house, or other out building." The Department contends that the words "by reason of his connexion with the land requires as a dwelling-house" mean that the proviso is only to apply to such portion, if any, of the building as should be needed as a dwelling house, store house or out building for the purpose of receiving of rents, or cultivation, or receiving of rent in kind as the case may be. The argument more shortly put is that the word "requires" is used in the sense of "needs" and that the words "by reason of his connexion with the land" mean as applied to this case "for the purpose of collecting the rent or revenue."

This interpretation, if correct, would leave the taxable proportion of the notional income from the building to be assessed by the Income-tax Officer as a matter of fact and without appeal. Now I can see no indication in the Act of any circumstances which are to guide the officer in assessing the taxable proportion. There is, for instance, no indication whether the dwelling house is to be of such a kind as to enable the owner to reside in it for such time as may be necessary for the collection by him of his rents, or whether his family may properly be expected to accompany him, or whether the distance from such other dwelling as he may own ought to be considered, or whether his social prestige or the need of displaying it to his tenants is to be taken into account. All these considerations and many others are according to the Department to be left to the officer as matters of fact within his sole discretion. Had this been the real intention of the Legislature one would have expected to find in the Act a set of guiding principles. On the other hand, for assessing the revenue of a business the Act provides elaborate guides. For this reason alone I am of opinion that the Legislature had no such intention as suggested by the Department.

But apart from this consideration the words of the proviso are not capable of the construction suggested. The word "requires" means that the assessee demands to appropriate the building for the purpose of a dwelling house, or as a store house, or other out building and the words "by reason of his connexion with the land" mean that only the fact of his being a receiver of rent or revenue,

or the fact of his being a cultivator, or the fact that he is a receiver of rent in kind entitles him to claim any building as a dwelling house, a store house or an out building. If he should not occupy any of these positions in connection with the land he is not entitled to claim, as tax free, accommodation of the kind specified. In other words, the expression "by reason of his connexion with the land" is merely used to explain the nature of the class of persons entitled to exemption. It has been said that punctuation must not be used in construing a statute other than as a mere *temporanea expositio*, and for this limited purpose it may be noticed that the words are not separated by a comma or otherwise from the words "the receiver of the rent or revenue or the cultivator or the receiver of the rent in kind," whereas the verb "requires" is separated by a comma from the grammatical subject and the phrase "by reason of his connection with the land." My conclusion is that this phrase has a qualitative and not a quantitative significance. Of course there must be a *bona fide* use of the building as a dwelling house, store house or out building and the assessee is not at liberty to claim arbitrarily the exemption of any building which he may at his own choice describe as a dwelling house, store house or out building without regard to the actual facts. For these reasons I am in agreement with the decision arrived at in the case of *Maharajadhiraja of Dhurbanga v. Commissioner of Income-tax*(1).

It has further been argued that the income on account of buildings which is to be exempted from taxation is not the notional income but the actual income, if any, derived therefrom. This argument will hardly bear examination, and I will say no more than that I am in full agreement with the views of my learned brethren on this point.

The next matter for decision is as to whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance is within the definition of agricultural income furnished by the Act, that is to say, "any rent or revenue derived from land which is used for agricultural purposes." It has been contended that the realisation of these mutation fees is illegal and unenforceable. To my mind this is not a circumstance, even if it be the fact, which has any bearing upon the question to be decided. The tenants are admittedly in occupation of agricultural land and however illegal the sum so collected it is paid by the tenant to the landlord by reason of the relationship of landlord and tenant of such land. Such being the case, the mutation fees paid are clearly income derived from land which is used for agricultural purposes and I agree with the former decision above referred to in which the same point was decided in favour of the assessee.

There was a third point as to the admissibility of deductions on account of interest paid on over-drafts but this point does not now call for consideration.

The answers to the questions put by the Commissioner being in favour of the assessee, he should receive 20 gold mohurs by way of costs.

ROSS, J.:—It is conceded that the first question is answered by the decision in *Maharajadhiraj of Dhurbhanga v. The Commissioner of Income-tax*(1), but it is argued that that case was wrongly decided. The learned Government Advocate advanced two alternative arguments.

The first was that this house property is taxable under section 9 and that no section of the Act exempts it from taxation. What is exempted by section 2 clause 1 (c) is income actually derived from a house of the kind therein referred to and as admittedly no income is actually derived from this house there is no exemption. There is more than one answer to this argument. What section 9

(1) 3 I. T. C. 158.

taxes is the annual value of buildings, and, where the buildings are in the occupation of the owner, rules are given for ascertaining the annual value to him, which is thus notional income and is taxed as such. But if notional income is taxable, it must also be subject to abatement of tax. Income cannot mean one thing for the purposes of taxation and another for the purposes of abatement. There is therefore no reason for restricting income in section 2 clause 1 (c) to income actually earned. Again, such a construction destroys the meaning of the clause. If a Zemindar lets his house, then he does not require it and therefore it is outside the clause altogether. It is suggested that what the clause refers to is income derived from letting part of the house; but the clause only exempts income from a building owned and occupied by the receiver of rent, and so far as it is not occupied by him, it is not within the exception.

The alternative argument was that advanced by the Commissioner of Income-tax that the house is too large for the assessee's requirements as a Zemindar and is therefore assessable in part. But if the legislature had contemplated such an inquisition into the domestic affairs of the assessee as this argument involves, it seems to me that it would have been expressly provided for. As was observed by Lord Hannen in *Tennant v. Smith*(1), income-tax is imposed not on the personal suitability of the man's surroundings which must vary with the man and the same man in different circumstances, but on his income capable of being calculated. There are three requisites for exemption under this clause: (1) the building must be owned and occupied by the receiver of the rent; (2) it must be on or in the immediate vicinity of the land; and (3) it must be a building which the receiver of the rent by reason of his connection with the land requires as a dwelling house. The first two conditions are admittedly satisfied, and the question is about the third; and this question reduces itself to the meaning of the word 'requires'. In my opinion the meaning is determined by the context and is limited only by the words immediately preceding and following it, namely, "by reason of his connection with the land" and "as a dwelling house." There is no reference, or suggestion of a reference, to the size of the house as a condition of exemption. The only test is that the receiver of rent has to occupy it as a dwelling house by reason of his connection with the land. If by reason of his connection with the land, he has to occupy that house (not a house as large as that), then the notional income derived from the occupation of that house is agricultural income and is exempt from taxation; otherwise the taxability of a Zemindar's house would vary with his zemindary income, the size of his family and his personal tastes. A house free of tax in the hands of one might be taxable in the hands of his successor and a house free of tax at one time might be taxable at another. In my opinion the answer to this argument is that these considerations are outside the Act and that a construction of the section which involves such considerations is not the true construction. I therefore see no reason to alter the opinion expressed in the judgment in *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax*(2), to which I was a party.

On the second question, it is conceded that so far as the mutation fees are fees payable on succession to tenures they are agricultural income; and this is said to be the result of section 14 of the Orissa Tenancy Act which entitles the landlord to a fee in the case of a transfer of a tenure by succession. But it is argued that mutation fees on the transfer of raiyati holdings by succession are not agricultural income because by section 30 of the Act the right of occupancy descends in the same manner as other immovable property in the case of intestacy and any fee taken for mutation of names is an illegal cess. I am unable to see

(1) 3 Tax. Cas., 158.; 1892) A. C. 150.

(2) 3 I. T. C. 158.

how the legality or illegality of a charge affects the source from which the income is derived. If a mutation fee on the transfer of a tenure is agricultural income, it is difficult to see on what principle the mutation fee on the transfer of a raiyati holding is not agricultural income also. In my opinion both these payments are equally revenue issuing from the land or, what is the same thing, from the relation of landlord and tenant.

Learned Counsel for the assessee pressed for a decision on the question of the legality of these charges. It is contended that section 30 merely states the rule of devolution of occupancy holdings in the case of intestacy and that the exaction of a mutation fee would be governed by custom, at any rate in a permanently settled estate. It is said that this custom has been recognized in the instructions of the Board of Revenue in 1893, and that it is followed by the Government itself as proprietor of the Khurda estate. This may be so, but the question seems to me to be altogether outside the jurisdiction of the Commissioner of Income-tax; and, consequently, not fit for decision by this Court in the present proceeding.

WORT, J.:—This is a case stated by the Commissioner of Income-tax under an order of this Court, dated the 22nd November, 1927. The Court required the Commissioner to state a case on three matters. As regards the third, however, the attitude adopted by the Commissioner before the order of the 22nd November 1927, appears to have been under a misapprehension of the facts and it has now been adjusted and the Crown concedes that the assessee is entitled to the deductions which were claimed in regard to this.

The remaining questions are two in number. The first is whether the house occupied by the assessee on his estate at Kanika is entitled to complete exemption as agricultural income under the provisions of section 2 sub-section (1) (c) and section 4 (3) (viii) of the Income-tax Act.

The second question that arises is whether certain mutation fees which are a part of the Zemindar's income are agricultural income within the meaning of section 2 sub-section (1) (a) of the Act.

It will be necessary in dealing with these points to state briefly the facts. The Raja of Kanika has a palace at Kanika which appears to have cost something like three lakhs of rupees apart from the zenana quarters. This palace is situated on his zemindari which is of an area of 439 square miles.

In the case stated it is admitted that the description of the palace complies with section 2 sub-section (1) (c) in that it is on or in the immediate vicinity of the land and that the building is owned and occupied by the assessee being the receiver of the rents and profits. The question which the Commissioner of Income-tax states arises is whether the whole valuation, that is, the annual value of the residence of this Zemindar should be exempted from income-tax regardless of the proportion between that valuation and his income from landed property and regardless further of the proportion which his income from landed property bears to his income from other sources. The Commissioner further states in the case that the assessee's income from rent proper is approximately 50 per cent. of his total income. Further he states that it is submitted that this palatial building is not required wholly and exclusively for agricultural purposes and that the question of valuation of what proportion of the total building the assessee should be assessed at is a question of fact in each case. The amount of the assessment of the building or a part thereof is undoubtedly a question of fact but nowhere in the Act does it provide that the dwelling house should be required for agricultural purposes. The Act uses the expressions "required as a dwelling house in connexion with the land."

The second section defines "agricultural income" and sub-section (1) (c) includes any income derived from any building owned and occupied by the receiver of rent or revenue of any such land, and eliminating irrelevant portions it goes on to provide that the building is on or in the immediate vicinity of the land and is a building which the receiver of the rent or revenue by reason of his connection with the land requires as a dwelling house, etc.

The question which arises is a question of mixed fact and law. But the real point before us, having regard to the findings of fact by the Commissioner, is what is the proper construction to be placed upon the words "required as a dwelling house in connection with the land."

The question has already come up before this Court and it has been decided in the case of *Maharajadhiraj of Dharbhanga v. The Commissioner of Income-tax, Bihar and Orissa*(1), that it is sufficient to show that by reason of the assessee's connexion with the land he requires a dwelling house in the vicinity and that it is not open to the Commissioner to consider whether the particular class of house is more or less the actual requirements of the Zemindar. One of the questions really before us is whether that case was rightly decided.

I have already indicated the view which the Commissioner takes with regard to the meaning of these words, and, in my judgment, clearly the test which he applies is a fallacious one.

It is important to notice that there is a statement by the Commissioner that the Income-tax Officer in making this assessment has taken Rs. 3,000 as the proportionate valuation of the portion of this palace which is not required for agricultural purposes. I would be content in founding my judgment on this statement or the inference to be drawn from it, having regard to the other facts which have been found in the case. This last statement, in my judgment, is tantamount to saying that the Raja requires this palace as a dwelling house in connection with the land, or to put it in other words, that having found that a portion of the building on the land is required for the purposes set out in the Act, the section has been complied with and that a Court is thereafter precluded from any further inquiry and that there is nothing in the Act to warrant his inquiring into what portion of the building is so required.

I have already stated that the Commissioner adds the words "required for agricultural purposes"; but there is no justification for these words "agricultural purposes" whatever. Equally there is no justification for the method which the Commissioner has adopted, namely, of testing the question by determining the proportion between "agricultural income" of the Zemindar to that of his total income.

However, as the question is really one as to the true construction of the Act, I propose to deal with the arguments which have been advanced with regard to it.

The first argument put forward by the learned Government Advocate on the construction of section 2 is one which is diametrically opposed to the contentions of the Income-tax Department, but that is immaterial, the contention being that when the word "income" is used in section 2 sub-section (1) (c) the meaning is actual income and not notional income: that is, income must mean actual money received as a profit from the building.

It is further contended in support of this argument that there is only one section in the Act which deals with notional income and that is section 9.

(1) 3 I T. C. 158.

It is obvious that the Crown must be driven back as it was to the contention that the exception under section 2 was not an exception to section 9.

For the purposes of this argument the Crown relies upon the case of *Tennant v. Smith*(1). The judgment in that case however gives no support to this argument. The judgment which related to the assessment of a bank manager under Schedule D of the Income-tax Act in England then in force, that is to say, the Act of 1842 and the question therein arising was whether the occupation of a house provided for him by his employees was an emolument within the meaning of that Schedule. The words in that judgment relied upon by the Crown are those in Lord Halsbury's speech "that the thing sought to be taxed is not income unless it can be turned into money."

The case as I have stated dealt with words quite different from those we have to construe. In effect the argument is this: that wherever the word "income" is used it means actual money or money's worth and not notional income in the sense of an annual value of a house occupied by the assessee. One answer to that argument is that the Income-tax Act as its name denotes deals with the taxation of income under several heads and one is "property" [Section 6 (iii)]. That so far as property is concerned notional income is taken. In other words section 9 (1) provides that the assessee in regard to Property shall be taxed on the *bona fide* annual value.

I think that statement is sufficient to meet the argument that actual income only is dealt with by the Act. The Crown in the case stated recognises this to be a case of notional income but says that it is an exception to the general meaning of the word income. But the plain construction of section 2 is a complete answer to the argument. The Act must be construed so as to give it a reasonable meaning. The effect of the construction contended for would be to repeal the provisions of section 2, or to make them a nullity. The dwelling house to be exempt must be owned and occupied by the receiver of the rents and profits of the agricultural land, and it must be required as a dwelling house. If it is occupied how can actual cash income accrue from it and indeed if it is occupied by a third person who will pay rent and thus render income to the owner, how can it be said that it is required as a dwelling house by the owner assessee. In my judgment this is an impossible construction.

The main argument however is that there must be some sort of relation or rather proportion to be fixed as between the dwelling house and the land or Zemindari and that is always a question of fact for the Commissioner. The words to be construed, therefore, are (substituting the phrases used so far as their positions in the section are concerned) "required as a dwelling house in connexion with the land". Now it is not argued that the Commissioner would be required, nor is he required, to enquire into the actual reasonableness of the demands of the Raja so far as the dwelling house is concerned. That is to say, he may live in any style he likes and have a palace or a hut. But it is said that the words "in connexion with the land" place limits upon or condition the Raja's requirements with regard to a dwelling house so far as the exemption from taxation is concerned. Do these words warrant any such argument? The Crown contends that the words warrant the following enquiries which the case stated suggests:—(i) Whether the assessee occupies the house *qua* landlord; (ii) What proportion does his income from land bear to his income from other sources; (iii) Whether the palace is required exclusively for agricultural purposes. The Crown contends as to (1) that the assessee does not occupy the house *qua* landlord. Then in what capacity does he occupy? In my judgment

(1) 3 Tax. Cas. 158.

in as much as he is entitled to a partial exemption according to the case stated he does in fact occupy the house *qua* landlord. That is to say that this or that part of the palace is not required by his occupation *qua* landlord or for agricultural purpose is either enquiring into the assessee's personal habits or tastes, an enquiry quite irrelevant on any construction to be placed upon the section, or to apply a test which the language of the Act in no way warrants. The section says requires as a dwelling house in connexion with the land, not requires as a dwelling house in connexion with and for the purposes of the land (or agriculture). If we were to read "for the purposes of agriculture" into the section which in effect the argument of the Crown contends for, the whole house would be outside the provisions of the section. Neither the dining room nor any of the living rooms are required in connexion with the land any more than the billiard room or zenanna quarters, placing the construction desired by the Crown upon the section.

In my judgment if the argument on behalf of the Crown is right then the construction contended for in the case stated is the only tenable one, that is, that only "Zamindari Kacherries, Manager's Offices and buildings of that nature" are exempt, and that contention is clearly wrong on any plain reading of the section, the sub-section stating as it does that dwelling house, or store house or other out buildings are exempt.

In my opinion the words we have to construe "in connexion with the land" merely make it necessary for the assessee to establish the relation between himself and his house with the land in order to claim exemption. Such relation in this case is established as a fact and in my judgment any further enquiry is precluded. The hypothetical case of a person building a palace on a few bighas of land with, say, one small holding seems hardly to touch the point. First such a case in India is unlikely to occur and secondly the case is so extreme that neither as a question of law or fact could it be stated that such a house was required as a dwelling house in connexion with the land: on the other hand the land would be required in connexion with the house or as one of its amenities, an exemption for which the statute does not provide. I would therefore hold that the case of *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax* (1), was rightly decided on this point and should be followed. In addition I think there can be no doubt that but for the exception contained in the sub-section under discussion, this palace would be taxable under section 9 as property. The assessee could not be heard to say that not all the palace was occupied by him and therefore not all of it should be taxed. The same construction should be placed upon the words under consideration whether they in fact involve exemption or taxation.

I see nothing in the Act to justify the argument that being required as a dwelling house yet only a portion is to be exempt.

The next point relates to the mutation fees. Sir Sultan Ahmad on behalf of the Crown admits that the basis of the Commissioner's contention so far as the fees secured by the Raja on the transfer of tenure was wrong and that the assessee is entitled to treat these as agricultural income within the meaning of the Act and therefore exempt. However his admission, as I understand it, goes only so far as the case in which the amount chargeable by the Raja is one which he is entitled by law to recover and not so far as any excess amount is concerned.

The other mutation fees are those realised from occupancy ryots and it is contended that as these are illegal *abwabs*, they can in no sense be termed revenue from land within the meaning of section 2 sub-section (1) (a).

In dealing with this latter point therefore I shall deal with that portion of the mutation fee on the transfer of tenures which is stated by the Crown to be illegal.

In the first place it was argued that the test which was to be applied in order to discover whether mutation fees could be treated as "agricultural income" within the meaning of the section, depended upon the question whether these fees were enforceable or not and this argument was supported by the case of *King Emperor v. Probhat Chandra Barua*(1), where it was decided that fees on petitions payable with regard to transferable holdings (as these were) were not "agricultural income." With this case I shall deal presently, but whether this authority decides that the legality of the fees is the real test, in my judgment it is impossible to say that the character of the fee is altered by the fact that it is irrecoverable; rent may be irrecoverable by reason of the fact that it is higher than the amount reserved in a lease, or that in an occupancy holding, an enhancement not allowed by the statute law is claimed. But the real character of both still remains, that of rent, and to repeat, to say that a thing is changed in character by reason of its being irrecoverable is beside the point.

It is contended by the respondent that mutation fees in respect of occupancy holdings were recoverable by means of a custom which existed for many generations past. But in the view that I take of the matter whether they are recoverable or irrecoverable is irrelevant in coming to a conclusion whether these fees are "agricultural income" and therefore that question had not been decided. The case which I have quoted and upon which the learned Government Advocate relies mentions the authority of *Meher Bano Khanum v. Secretary of State for India*(2), and the learned Judges deciding that case have differentiated the case of *Birendra Keshore v. Sec. of State*(3), on the ground that what the learned Judges were referring to was *nazar* which was paid by a tenant for the recognition of a transfer of a non-transferable occupancy holding and that in effect *salami* or *nazar* paid in those circumstances really amounted to the capitalised value of a part of the rent for a new settlement. In my judgment, quite clearly, if that was the basis of the decision in the case of *Meher Bano Khanum v. Secretary of State for India*(2), then what the Court was there deciding was that *nazar* was rent, for the reason that capitalised rent is rent.

The question which we have to determine is whether these fees are rent or revenue within the meaning of section 2 sub-section (1) (c) and these fees do not cease to be revenue by reason of the fact that *nazar* was capitalised rent. These fees are not rent.

One of the questions, therefore, for determination is whether the Legislature in using the expression "rent" or "revenue" intended by the word "revenue" something other than "rent". In my opinion the word "revenue" is not to be construed as *ejusdem generis* with rent. "Rent" has characteristics which are well known to lawyers. "Revenue" whilst it may be a species of agricultural income has, in my judgment, a wider meaning than rent.

Now from what source do these fees come? Is it by reason of the relation that the person recovering them has with the land? I think this question

(1) 2 I.T.C. 392.

(2) 2 I.T.C. 99.

(3) 1 I.T.C. 67.

must obviously be answered in the affirmative; and apart from the fact that they may not be recoverable in law, I do not see any distinction, between *nazar* and or *salami* in the case of a tenure and the fee paid with regard to occupancy holdings. If the former is "revenue", I do not see how it can be argued that the other is not revenue as well. In this connection it is important to notice again that what the case of *King Emperor v. Probhat Chandra Barua*(1), has decided is that *nazar* was revenue although the reason which is given in the case of *Meher Bano Khanum v. Secretary of State for India*(2), for that decision is that *nazar* was in the nature of rent. It is not suggested before us that the fees in this case are rent, but it is argued it is not revenue. If that is the *ratio decidendi* of the case of *Meher Bano Khanum v. Secretary of State for India*(2), then it would appear to be of no assistance to us in determining the question of whether these fees are revenue within the meaning of section 2.

The Oxford Dictionary definition of the word "revenue" has been referred to in the case stated but I see no support for the Crown's argument from that definition; the definition is a return, yield, or profit of any land, property or other sources of income. Can it be doubted for a moment that this is a return or yield or profit from property or landed property? It is undoubted that but for the ownership of this land, this source of income, using that word in a neutral sense would not be available to the assessee. I would hold, therefore this is agricultural income in the sense that it is revenue from land.

In my judgment, all the points which are before us should be answered in favour of the assessee, that is to say, that on the facts proved or admitted the whole of the palace at Kanika should be exempt under section 2. The fees on the transfer of tenures and the fees for the mutation of names with regard to occupancy holdings are agricultural income within the meaning of the section referred to.

KULWANT SAHAY, J.:—The questions which arise for determination in this reference under section 66 of the Income-tax Act are:—(1) whether any portion of the valuation of the assessee's palace at Kanika is taxable, or, whether on the other hand, the whole valuation of this palace should be exempted as being agricultural income within the meaning of section 2 (1) (c) of the Act; (2) whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance are covered by the term "agricultural income" as defined in section 2 of the Act and (3) whether the assessee can be allowed as an admissible deduction the amount of interest which he has paid on overdrafts during the "previous year."

As regards the first point: section 4 (3) sets out the classes of income to which the Act shall not apply, and one of these classes is agricultural income. "Agricultural income" is defined in section 2 (1) of the Act. Section 2 (1) (c) makes income derived from any building owned and occupied by the receiver of the rent or revenue of any such land, or occupied by the cultivator, or the receiver of rent-in-kind, of any land with respect to which, or the produce of which, any process mentioned in sub-clauses (ii) and (iii) of clause (b) is carried on. To this there is a proviso to the effect that the building is on or in the immediate vicinity of the land and is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land, requires as a dwelling house, or as a store-house, or other out-building. The question is whether the assessee can rely upon this proviso for exemption of his house from taxation. Section 6 of the Act gives the heads of income, profits and gains which shall be chargeable to income-tax in the manner

provided in the Act, and one of these heads is "property." The manner in which 'property' is chargeable to income-tax is given in section 9, sub-section (1) of which provides that the tax shall be payable by an assessee under the head "property" in respect of the *bona fide* annual value of the property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of his business, subject to certain allowances set out in the section. In the case of buildings in the occupation of the owner it is the notional income upon which the tax is to be payable. It is contended on behalf of the Crown that the house in question in the present case is taxable under section 9, and that what is exempted by section 2 (1) (c) is income actually derived from any building owned and occupied by the receiver of the rent or revenue and does not include the notional income of the building. In my opinion this contention is unsound and cannot be accepted. Section 2 (1) of the Act gives the definition of "agricultural income," and chapter III, deals with taxable income; section 6 gives the heads of income and section 9 provides for the mode of determining the income taxable under the Act under the head "property." Such income under section 9 in respect of buildings in the occupation of the owner must be notional income, and the argument of the learned Government Advocate that what is exempted by section 2 (1) (c) is actual income is contrary to the provisions of the Act itself.

The real question, however, for determination is what is the meaning of the proviso to section 2 (1) (c). In order that the income derived from any building may be held to be agricultural income, it is necessary that the building must be (1) on or in the immediate vicinity of the land and (2) it is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land requires as a dwelling house or as a store-house or other out-house or other out-building. It is conceded in the present case that the building in question is on or in the immediate vicinity of the land. It has been found by the Commissioner as a fact that a part at least of the building is required by the receiver of the rent or revenue as a dwelling house, by reason of his connection with the land. The question is whether there is any justification in the Act for the Commissioner to decide what portion of the building the assessee does in fact require as a dwelling-house by reason of his connection with the land. In my opinion, the moment it is found that the building or any portion of it is required by the receiver as a dwelling house the income derived from such building would become agricultural income and exempt from taxation. The argument that the word "requires" gives the Income-tax authorities the power to determine what portion of the building is as a matter of fact required by the assessee in his capacity of receiver of the rent is, in my opinion, not warranted by the terms of the section. I agree with the reasons given by my Lord the Chief Justice and by Ross and Wort, JJ., for holding that the construction sought to be placed upon the proviso by the Income-tax authorities is not warranted by the terms of the section. It would no doubt be open to the Income-tax authorities to hold that a particular building on account of its size or situation is not a building which the receiver of rent or revenue does require, by reason of his connection with the land, as a dwelling house and in that case it would be open to them to assess the income from the entire building, but the moment they find that the house is required by the receiver of the rent or revenue by reason of his connection with the land as a dwelling house or a store-house or other out-building, it is beyond their jurisdiction to determine what portion of the building is or should be required by the assessee as such receiver of the rent or revenue. In my opinion the case of *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax*(1), was

correctly decided and I would answer the first part of the first question in the negative and the second part in the affirmative.

As regard the second point: I agree for the reasons given by my Lord the Chief Justice and by Ross and Wort, JJ., that mutation fees paid by tenants upon succeeding to holdings or tenures are covered by the term "agricultural income" as defined in section 2 of the Act. The question whether such fees are legally recoverable or not is a question beyond the jurisdiction of the Income-tax authorities. The words "rent or revenue derived from land which is used for agricultural purposes" in section 2 (1) (c) of the Act are wide enough to cover receipts by landlords in the shape of mutation fees.

As regard the third point: the learned Commissioner finds that the assessee is entitled to claim deduction of the amount of interest which he has paid on overdrafts during the previous years and the question does not arise for determination.

MACPHERSON, J.:—Under section 66 of the Indian Income-tax Act, 1922 the Commissioner of Income-tax has, as required by this Court in its order of the 22nd November, 1927, stated a case on three questions and referred the same to this Court with his own opinion thereon. The assessee is the proprietor of the Kanika estate in Orissa.

The first question is whether any portion of the valuation of the assessee's palace at Raj-Kanika is taxable, or whether on the other hand the whole valuation on this palace should be exempted as being agricultural income within the meaning of section 2 (1) (c) of the Act. The facts are briefly these. The gross income of the assessee comes to Rs. 3,90,000, of which income from agricultural rent is approximately Rs. 2,10,000. The Manager's office which also houses the Zemindari staff is a separate and older building. In the palace proper only seven of the Zemindari staff are accommodated and practically the whole of the building is used as a residence for the assessee and for visitors. It was built in 1912 at a cost of Rs. 3,00,000 and zenana quarters were subsequently added at a cost of Rs. 1,00,000. It has the ordinary accommodation of a palace and there is a detached guest-house. The Commissioner states: "The Income-tax Officer in making the assessment has taken Rs. 3,000 as the proportionate valuation of the portion of the palace which is not required for agricultural purposes." It would appear that the expression "requires for agricultural purposes" here means "which the assessee by reason of his connection with the land requires as a dwelling house."

The Commissioner sets out that it is the contention of his department that the palace is not occupied by the receiver of rent, nor required by him *qua* landlord as a dwelling house, store-house or other out-building. The assessee's income from rent proper is approximately fifty per cent. of his total income and it is contended that "the assessee requires or has built his palatial residence not because he requires such a building by reason of his connection with the land but because his total income and high social position demand." The Commissioner submits that "this palatial building is not required wholly and exclusively for agricultural purposes and that the question of the valuation of what proportion of the total building assessee should be assessed is a question of fact to be decided in each case," regard being had in coming to a decision to the provisions of the proviso to section 2 (1) (c) of the Act and in particular to the point whether the building in question or the whole of the building is required (as dwelling house) by reason of the assessee's connection with the land. The assessee, he repeats, has been taxed only on a small portion of the annual valuation of the palace proper.

The short point therefore is whether the palace proper is a building which the assessee (who is admittedly the receiver of the rent or revenue derived from the land of Kanika estate which is used for agricultural purposes and which is assessed to land-revenue in British India) by reason of his connection with the land requires as a dwelling house. If it is such a building, the annual value of it is agricultural income and the Act does not apply to it as admittedly it is on the land; if it is not such a building, the Act applies.

Now the proviso to section 2 (1) (c) limits the building owned and occupied by the assessee the valuation of which is agricultural income under the definition, to a building of the class described in the proviso—it must be one which the receiver of the rent or revenue of the land by reason of his connection with the land requires as a dwelling house. The submission on behalf of the assessee is practically that this proviso is satisfied if the building is one *which or a part of which* the receiver of the rent or revenue of the land by reason of his connection with the land *uses* (or even states that he uses) as a dwelling house. But such does not appear to be the intention. It is indeed not even arguable that mere use or allegation of use or even allegation of need satisfies the proviso. It is sufficient therefore to discuss the case where the building is one a part only of which the assessee by reason of his connection with the land *requires* as a dwelling house where the word 'requires' is taken as equivalent to 'needs'. Now if the Legislature had contemplated that the assessee's requirement by reason of his connection with the land of a part merely of the building as a dwelling house would be sufficient, what prevented it from saying that? The connotation of the expression "by reason of his connection with the land requires" must be "needs as appropriate and convenient for his calling as a receiver of the rent or revenue derived from the land." The learned Counsel for the assessee would practically read the proviso (so far as is material) as "Provided that, the receiver of the rent or revenue by reason of his connection with the land requires a dwelling house." But the enactment contemplates that he must by reason of his connection with the land require the particular building as a dwelling house. In this Province the case of the great Indigo concerns of North Bihar readily occurs to one. The residence of the owner or manager was appropriate to the extensive landed interests of the Concern. But it is otherwise when on the dissolution of the Concern that building is acquired with some neighbouring land constituting but a small fraction of the territory of the Concern and is occupied by the purchaser mainly not by reason of his connection with the adjoining land but for merely residential reasons, or from considerations of local prestige, or for sporting purposes, or some similar object. The Legislature cannot have intended to exempt such purchasers from income-tax on the building. To my mind language has been employed which indicates an intention to discriminate between the requirements of the assessee as the landlord and his requirements as an individual. In the present instance it is found as a fact that the whole palace is not a building which the assessee as receiver of the rent or revenue of the land "by reason of his connection with the land requires as a dwelling house," and accordingly it is not such a building as is described in section 2 (1) (c) read with the proviso and therefore the notional income thereof is not agricultural income so as to be under section 4 (3) (viii) outside the application of the Act. Strictly therefore the whole palace falls within section 9 and it was apparently open to the Commissioner to assess the notional income from it accordingly. No doubt the Income-tax department has further found that a portion of the palace comes within the proviso and it has not assessed the income from such portion to income-tax. But we are not concerned here with the attitude of the department in taking what may be less than its full right, except to this extent that if, as is contended (in my opinion erroneously) the total annual value of the whole palace and not the proportionate value of the portion not required as a dwelling house by the receiver of the

rent or revenue of the land, is Rs. 3,000, the assessment would still not be illegal. It is however sufficient in the present reference to answer the first portion of the question in the affirmative and the second portion in the negative. In my opinion the reference in *Maharajadhiraj of Darbhanga v. The Commissioner of Income-tax, Bihar and Orissa* (1), was not correctly decided.

The second question is whether mutation fees paid by the assessee's tenants upon succeeding to holdings or tenures by inheritance come within the definition of 'agricultural income' as defined in the Act, so that the Act does not apply to them. As admittedly the land is assessed to land-revenue in British India, the point shortly is whether these fees come within the expression "any rent or revenue derived from land which is used for agricultural purposes." The tenants referred to are of two classes: (1) tenure-holders, and (2) raiyats.

A tenure-holder pays the fee under section 14 of the Orissa Tenancy Act. The Commissioner points out that the fee is not within the definition of 'rent' under that Act and indicates that if the expression 'revenue' is to be taken in so wide a sense 'agricultural income' would include illegal realisations, such as *abwabs*. This however does not appear to be the correct criterion, since 'rent' in the Tenancy Act has by definition a restricted meaning appropriate to such an enactment but inappropriate to an Income-tax Act, and the learned Government Advocate is unable to contend that the fee paid by a tenure-holder to the landlord under the statute is not "rent or revenue derived from the land" and therefore "agricultural income."

As to the succession fees paid by the raiyats in this permanently settled estate, the Commissioner considers that they are illegal impositions under section 84 of the Orissa Tenancy Act, the exaction of which is punishable by fine under section 83. In short "the landlord is charging a fee for keeping his jamabandi up to date, which it is his duty to do without any fee", and the payment is therefore one without consideration.

Here again the chief fallacy appears to lie in the Commissioner's assumption that the expression 'rent' in the Income-tax Act, 1922, has the same meaning as it has in the Orissa Tenancy Act. Payments to the landlord which are not 'rent' under the Tenancy Act which term is as usual in such enactments defined for the purpose of the Act as "whatever is lawfully payable.....", may well be 'rent' derived from the land within the meaning of the Income-tax Act, where not the legality or morality but the character and origin of the income are in point.

It has been urged, not very convincingly perhaps, that the payment is even 'rent' within the meaning of the term in the Tenancy Act but it is not necessary to determine the point. The small fee legally or illegally paid by a raiyat to his landlord for the mutation in the landlord's papers of his name by virtue of succession appears not to be a mere payment for a service but to fall within the wide expression "rent or revenue derived from the land," irrespective of any dissection of the individual terms 'rent' and 'revenue'. I would answer the question in the affirmative.

The third point is whether the assessee can be allowed as an admissible deduction the amount of interest which he has paid on certain overdrafts during the 'previous year.' The Commissioner points out that the assessee can be allowed interest for 1924-25 on Rs. 501-4-0, borrowed on the 13th October, 1923, and a deduction of interest which accrued on Rs. 3,030 in the period 22nd October 1924 to 31st March 1925. There is no controversy on this point and I would answer it in the affirmative.

(313) IN THE HIGH COURT OF JUDICATURE AT LAHORE.
FULL BENCH.

*Before Mr. Justice A. B. Broadway, Mr. Justice Cecil Fforde, and
Mr. Justice Zafar Ali.*

(31st May, 1929).

Bhagat Dunichand of Haripur

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and North-
West Frontier Province

.. Referring Officer.

*Income-tax Act, (XI of 1922), Secs. 23 (4) and 30—Assessment under
Sec. 23 (4)—Assessee claiming to be a non-resident—Assessment appealed as ultra
vires—Proviso to Sec. 30, if bars appeal.*

*An appeal against an assessment under Sec. 23 (4) on the ground that the
assessee as a non-resident of British India was not liable to be assessed under the
Act is barred by proviso to Sec. 30 (1), provided the assessment was a genuine
and not an ostensible one.*

*The proviso makes no distinction between an ultra vires assessment and an
intra vires assessment objected to on the merits.*

Case [Civil Reference No. 21 of 1928], stated under Sec. 66 (3) of the
Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax,
Punjab and N. W. Frontier Province in compliance with the order of the High
Court, dated 6th February, 1928, reported as 3 I. T. C. 52.

CASE.

By an order dated the 6th February 1928, I have been required by the
Hon'ble High Court under Sec. 66 (3) of the Indian Income-tax Act, (XI of
1922), to refer to it the following question of law with my opinion thereon: "Was
the Assistant Commissioner bound to decide whether Bhagat Duni Chand was
or was not a resident of British India, or does the proviso to Sec. 30, bar an
appeal on the question of liability to assessment when action has been ostensibly
taken under section 23 (4)?"

2. The main facts of this case have already been stated in the order
made by the Hon'ble Judges. The petitioner, Bhagat Duni Chand, owns house
property and investments at Haripur in the Hazara District of the N. W. F.
Province and also carries on business in Kashmir. He had for several years
been assessed to income-tax (1) on the income from his property and investments
in Haripur and (2) on that part of the profits and gains of his Kashmir business
which is received or brought into British India and which under Sec. 4 (2)
of the Act is deemed to have accrued or arisen in British India. In the assess-
ment proceedings of the year 1924-25, the Income-tax Officer of Hazara served
on the petitioner a notice under Sec. 22 (4) of the Act requiring him to produce
the accounts relating to his Kashmir business, in order that that Officer might
determine what portion of the profits had been remitted to British India and
had become liable to income-tax under Sec. 4 (2). The petitioner did not comply
with this notice, but claimed that he was not a resident of British India, and
was not liable to be taxed on any part of his Kashmir profits. The Income-tax

* (1929) 10 Lah. 596. A. I. R. (1929) Lah. 593.

Officer examined this contention of the petitioner and rejected it. Thereupon, as the petitioner had failed to comply with the notice under Sec. 22 (4), the Income-tax Officer proceeded to make the assessment under Sec. 23 (4) to the best of his judgment. The assessee appealed from this assessment to the Assistant Commissioner and took the ground, among others, that he was not a resident of British India. The Assistant Commissioner, holding that no appeal lay from an assessment under Sec. 23 (4), refused to entertain it. A petition to the Commissioner for review of the assessment under Sec. 33 was also rejected.

3. My opinion on the question, which I have been asked to refer, is that the first part should be answered in the negative, and the second in the affirmative, that is to say, I consider that the Assistant Commissioner was not bound to decide whether Bhagat Duni Chand was or was not a resident of British India, and that the proviso to Sec. 30 bars an appeal on the question of liability to assessment, when an assessment has been made under Sec. 23 (4). The High Court has framed the last clause of the question as follows: "When action has been ostensibly taken under Sec. 23 (4)." I have not adopted this phrasing in giving my opinion for reasons which will appear in para 6 below.

4. Sec. 30, clause (1) of the Act says that "any assessee objecting to the amount or rate at which he is assessed under Sec. 23 or Sec. 27, or denying his liability to be assessed under this Act, or objecting to a refusal of an Income-tax Officer to make a fresh assessment under Sec. 27, or to any order against him under sub-section 2 of Sec. 25 or Sec. 28, made by an Income-tax Officer, may appeal to the Assistant Commissioner against the assessment or against such refusal or order: Provided that no appeal shall lie in respect of an assessment made under sub-section (4) of Sec. 23, or under that sub-section read with Sec. 27."

It is clear that there are four types of appeal contemplated here: viz., (1) an objection against the amount or rate at which the appellant has been assessed, (2) a denial of liability to assessment under the Act, (3) an objection to a refusal of the Income-tax Officer to re-open the assessment, and (4) an objection to an order made under Sec. 25 (2) or Sec. 28. These four types of appeal are recapitulated in the last words of the first sentence of the clause "may appeal to the Assistant Commissioner against the assessment or against such refusal or order." It is clear that the first two types of appeal are designated appeal "against the assessment."

Now the proviso stated in the most categorical terms that "no appeal shall lie *in respect of* an assessment made under sub-section 4 of Sec. 23." These words, even on the narrowest interpretation, cannot mean less than that an assessee cannot appeal "against an assessment" made under the sub-section specified. In my opinion, there is no possible room for doubt as to the plain meaning of the proviso. Had the legislature intended that an appeal on the question of liability should not be barred, it would have been a perfectly simple matter to exclude this kind of appeal from the scope of the proviso, which could quite easily have been confined to appeals against the amount or rate at which the tax-payer had been assessed, or against any penalties imposed on him under Sec. 25 (2) or Sec. 28. The use of the phrase "in respect of" clearly bars any attempt to confine the application of the proviso to particular aspects of the kind of assessment in question.

5. If we turn from a close scrutiny of the words employed in the Act to the larger aspects of the question, it will be found that the question of liability can be raised in so many ways that it would on any other interpretation be easy for an assessee, who by his own default had rendered himself liable to an assessment under Sec. 23 (4), to frustrate the intention of the proviso to

Sec. 30 (1) and claim a reconsideration by the Assistant Commissioner which would, of necessity, go into the merits of the assessment. Thus in the present case the assessee, besides taking the ground that he is not a resident of British India, could take the ground that the income taxed does not consist of the profits or gains of a business at all, or that they were never received or brought into British India, or that they were not received or brought into British India within three years of the end of the year in which they accrued or arose. All or any of these contentions directly affect the liability of the assessee under Sec. 4 (2) of the Act. Similarly, in the more common case where income is liable under Sec. 4 (1) the assessee could claim that the income taxed did not accrue or arise at all, or was not received, or that it did not accrue or arise in British India. Finally, clause (3) of Sec. 4 enumerates eight classes of income to which the Act does not apply. Most of these claims could only be decided by a careful examination of the accounts, and it would be manifestly absurd to hold that a man who had deliberately refused to produce his accounts was entitled to a reconsideration of the only kind of assessment which it was open to the Income-tax Officer to make, and which, in fact, he is by the law compelled in the circumstances to make.

6. The remedy which the Act provides for an injustice inflicted by an assessment under Sec. 23 (4) is an application under Sec. 27 to the Income-tax Officer to cancel the assessment. If the Income-tax Officer is not satisfied that the assessee was prevented by sufficient cause, or had not a reasonable opportunity to comply with the relevant requirements and refuses to re-open the case, then it is open to the assessee to appeal to the Assistant Commissioner under Sec. 30 (1) against the refusal of the Income-tax Officer to make a fresh assessment. Apart from this special machinery, it is also open to an assessee to move the Commissioner to exercise his power of revision under Sec. 33. (The assessee can, of course, file a civil suit if the Income-tax Officer's action is entirely without jurisdiction). When, however, as in the present case, resort is not had to Sec. 27, the Assistant Commissioner has no authority to entertain an appeal under Sec. 30. If such an appeal is made, the Assistant Commissioner can only consider whether the Income-tax Officer applied his mind to the relevant questions before making the assessment under Sec. 23 (4). If the Income-tax Officer *did* so apply his mind, the Assistant Commissioner has no power to entertain the appeal. If, however, the Income-tax Officer did not apply his mind to the relevant questions, the Assistant Commissioner can interfere, because it is not really an assessment under Sec. 23 (4) at all, but has been merely labelled so by the Income-tax Officer. It is for this last reason that I would respectfully submit that the question framed by the High Court should be slightly modified in its last words. An assessment ostensibly made under Sec. 23 (4) might possibly be found to be an assessment which is merely labelled such, although the Income-tax Officer had not applied his mind to the relevant questions which arise under that sub-section and which must be answered before an assessment under that sub-section is made. In such wrongly labelled cases, the Assistant Commissioner would be entitled to interfere and to entertain the appeal on its merits. The present case was, however, not such a case. It is clear from the assessment order that the reason why the assessment was made under Sec. 23 (4) was the assessee's failure to produce accounts, and it was never denied that he had been duly served with a notice under Sec. 22 (4) for the production of them. The Income-tax Officer had moreover carefully applied his mind to the question raised by the assessee regarding his liability to assessment, and had decided that he was liable. Such being the case, he was, in view of the assessee's default in producing accounts, compelled to make the assessment under Sec. 23 (4). These facts again left no ground to the Assistant Commissioner for interference, when an appeal was presented to him under Sec. 30, and he rightfully refused to entertain it.

7. I, therefore, submit that the answer to the question referred is that the proviso to Sec. 30 (1) bars an appeal against an assessment under Sec. 23 (4) on any ground whatever, and that in the present case, the Assistant Commissioner had no jurisdiction to consider whether Bhagat Duni Chand was or was not a resident of British India.

Mehr Chand Mahajan, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

Reference to Full Bench.

ZAFAR ALI AND JAI LAL, JJ.:—This reference under section 66 (3) of the Income-tax Act, (XI of 1922), has been made by the learned Commissioner of Income-tax in compliance with an order of a Division Bench of this Court, dated the 6th February 1928.

The assessee on whose application the said order was passed is Bhagat Duni Chand whose ancestral home is at Haripur, a town in the North West Frontier Province, and he owns there some house property also. He, however, asserted that he had migrated from Haripur to Srinagar in Kashmir and had long been residing and carrying on business there and had thus ceased to be a resident in British India. The Income-tax Officer of the Hazara Circle, which comprises Haripur, did not accept this plea and he served on *Bhagat Duni Chand* a notice under section 22 (4), requiring him to produce his accounts, etc., relating to his business in Srinagar. As *Bhagat Duni Chand* omitted to do so, the Income-tax Officer made an assessment under section 23 (4) to the best of his judgment. *Bhagat Duni Chand* then appealed to the Assistant Commissioner to urge that the Income-tax Act was not applicable to him because he was not a resident of British India. The Assistant Commissioner held that the appeal was incompetent, in as much as the assessment had been made under section 23 (4) of the Act.

Bhagat Duni Chand contends that he is entitled to an adjudication by the Assistant Commissioner on his plea that he is not a resident in British India and is therefore not liable to be assessed in British India.

The question which the Commissioner was directed to refer was: "whether *Bhagat Duni Chand* was or was not a resident of British India, or does the proviso to section 30 bar an appeal on the question of liability to assessment when action had been ostensibly taken under section 23 (4)."

The answer to this question depends entirely on the interpretation of clause (1) of section 30 with the proviso attached thereto. This clause (1) gives right of appeal to an assessee who (1) objects to the amount or rate at which he is assessed under section 23 or 27, or (2) denies his liability to be assessed under the Act, or (3) objects to the refusal of an Income-tax Officer to make a fresh assessment under section 27, or (4) objects to any order against him under sub-section (2) of section 25 or section 28 made by an Income-tax Officer.

The proviso denies the right of appeal to a person who has been assessed under sub-section (4) of section 23, or under that sub-section read with section 27.

It is contended on behalf of the assessee that he is "outside the Act"; in other words that he is not amenable to it. On the other hand it is urged on behalf of the Income-tax Commissioner that the expression "denies his liability to be assessed under the Act," is wide enough to cover the case of a person like the present assessee and, therefore, that such a person is not entitled to

appeal except as laid down in section 30. It is argued that the right to appeal does not exist in the nature of things but is always a creature of legislation.

The question, in our opinion, is eminently one for a reference to a Full Bench owing to its importance and the possibility of the correctness of either view. We, therefore, direct that the case be placed before the learned Chief Justice to constitute a Full Bench for the hearing of this reference.

SHADI LAL, C. J.:—Let the case be heard by a Full Bench.

JUDGMENT.

The question of law, which we have to determine may be formulated in the following terms:—Whether a person, who has been assessed by the Income-tax Officer under section 23 (4) of the Indian Income-tax Act, (XI of 1922), is entitled to prefer an appeal to the Assistant Commissioner on the ground that he was not liable to be assessed under the Act; or whether the proviso to section 30 (1) operates as a bar to his appeal.

It is common ground that in the proceedings before the Income-tax Officer the assessee put forward the claim that he had migrated from Haripur in British India to Srinagar in the Jammu and Kashmir State, and had been residing and carrying on business at the latter place. He accordingly urged that he had ceased to be a resident in British India, and that, as no income, profits or gains had accrued or arisen to him, or been received by him, in British India he did not come within the ambit of the Act. The Income-tax Officer did not accept this plea, and served on him a notice under section 22 (4) requiring him to produce certain accounts. The assessee did not comply with the notice, and the Income-tax Officer thereupon made an assessment under section 23 (4) to the best of his judgment. The question arises whether the assessee can appeal to the Assistant Commissioner against the assessment, or whether his right of appeal is barred under the proviso to section 30 (1).

The doctrine is well-established that there is no inherent right of appeal, and that a right of appeal must be given by a statute or by some authority equivalent to a statute. Now, section 30 (1) which deals with the right of appeal in cases under the Indian Income-tax Act provides that "any assessee objecting to the amount or rate at which he is assessed under section 23 or section 27, or denying his liability to be assessed under this Act, or objecting to a refusal of an Income-tax Officer to make a fresh assessment under section 27 or to any order against him under sub-section (2) of section 25 or section 28, made by an Income-tax Officer, may appeal to the Assistant Commissioner against the assessment or against such refusal or order." The right conferred by this sub-section is, however, subject to the proviso that 'No appeal shall lie in respect of an assessment made under sub-section (4) of section 23, or under that sub-section read with section 27.'

The reason for enacting this proviso is obvious. The law punishes a person who does not comply with the requisition of an Income-tax Officer by depriving him of his right of appeal. But the appellate authority must, before denying him the right of appeal, be satisfied that he had really incurred the penalty prescribed by the law, and that the Income-tax Officer had acted legally in assessing him under section 23 (4) of the Act. The mere fact that the assessment purports to have been made under that sub-section does not shut out the appeal; it must be shown that the circumstances of the case bring it within the scope of that sub-section. When the Assistant Commissioner is satisfied that the assessment was made, not ostensibly but genuinely, under that sub-section,

he must stay his hands and decline to adjudicate upon the merits of the appeal on the short ground that the proviso to section 30 (1) bars an appeal in such a case. And it is immaterial whether the order of the Income-tax Officer is impeached on the ground that the assessee was not amenable to the provisions of the statute, or on any other ground mentioned in the sub-section. The language of the sub-section makes it clear that the denial of his liability to be assessed under the Act can be put forward by the assessee as a ground of attack against the assessment; but that ground, just as any other ground specified in the sub-section is open only to a person who has not incurred the penalty prescribed by the proviso.

It is contended by the learned counsel for the assessee that, though his client is debarred by the proviso from challenging the assessment on the merits, he is entitled to show that he was outside the statute and that the Income-tax Officer had absolutely no jurisdiction to proceed against him. There is, however, no warrant for making this distinction. The proviso shuts out an appeal in every case in which the assessment has been made under section 23 (4), and makes no distinction between an assessment, which is *ultra vires*, and one which though *intra vires*, is wrong on the merits. If once the appeal is barred, the assessee cannot avail himself of any ground of appeal whatever may be the category to which it belongs.

It is possible, as argued by Mr. Mehr Chand Mahajan, that this view of the law may result in hardships in some cases. Suppose a foreigner comes to India as a visitor, and, when called upon by an Income-tax Officer to make a return of his income he fails to comply with the requisition in the belief that, as he was not carrying on any business in British India, he was not liable to be assessed to income-tax under the Indian Law. If the Income-tax Officer assesses him to income-tax under section 23 (4), the assessee has no right of appeal against the assessment, though it is palpably wrong. It is true that section 27 provides him with a remedy to re-open such an assessment, but the remedy is a precarious one and cannot be invoked unless he proves to the satisfaction of the Income-tax Officer that he was prevented by sufficient cause from making the return. If the assessment is *ultra vires* the aggrieved person may perhaps bring a suit for a declaration that it is illegal; Vide *Haji Rehemtulla Haji Tirmahomed v. The Secretary of State for India*(1).

Be that as it may, it is for the legislature to provide a remedy for cases of hardship if any. The duty of the courts is to enforce the law as they find it and they cannot allow their interpretation of the law to be influenced by any extraneous circumstance.

I have bestowed upon the matter my careful consideration and reached the conclusion that the assessee has no right of appeal against the assessment made under section 23 (4) by the Income-tax Officer, and that he is prevented by the proviso to section 30 (1) from showing that he was not liable to be assessed under the Indian Income-tax Act.

BROADWAY, J.:—One *Bhagat Duni Chand* was a resident of Haripur in the District of Hazara in the North West Frontier Province. He possessed there certain ancestral property. He was called upon by the Income-tax Officer of the Hazara Circle to furnish a return for purpose of income-tax. He failed to comply with this demand, asserting that he had migrated from Haripur to Srinagar in Kashmir many years ago, that he was carrying on his business in the Kashmir State alone and was no longer a resident of British India. The Income-tax Officer held that Duni Chand was still a resident in British India and had a business at Haripur from which he derived an income. A notice

under section 22 (4) of the Income-tax Act was served on him calling on him to produce accounts. As he failed to comply with this notice, the Income-tax Officer took action under section 23 (4) of the Income-tax Act and assessed him on an income of Rs. 17,669 at the rate of 9 pies in the rupee.

Against this assessment, *Bhagat Duni Chand* preferred an appeal to the Assistant Commissioner who dismissed the appeal holding that it fell within the purview of the proviso to section 30 of the Income-tax Act and was therefore not competent.

Bhagat Duni Chand thereupon moved the Commissioner of Income-tax to make a reference to the High Court. This was refused on the ground that no point of law was involved. Thereupon *Bhagat Duni Chand* came up to this Court under section 66 (3) of the Income-tax Act and a direction was issued by a Division Bench on the 6th February, 1928, directing the Commissioner to refer the following question:—"Was the Assistant Commissioner bound to decide whether *Bhagat Duni Chand* was or was not a resident of British India, or does the proviso to section 30 bar an appeal on the question of liability to assessment when action has been ostensibly taken under section 23 (4)."

In compliance with this direction, the Commissioner of Income-tax made the necessary reference, at the same time recording his opinion against the view advanced by *Bhagat Duni Chand*. In his opinion the Assistant Commissioner was not bound to decide whether *Bhagat Duni Chand* was or was not a resident of British India, and further he considered that the proviso to section 30 barred an appeal on the question of liability to assessment when an assessment has been made under section 23 (4).

In his reference the Income-tax Commissioner also pointed out that when an assessment was made under section 23 (4) the assessee has a right to make an application to the Income-tax Officer under section 27 for cancellation of the assessment, and a refusal on the part of the Income-tax Officer gives the assessee a right of appeal to the Assistant Commissioner. In addition to this the Commissioner of Income-tax has certain powers of revision under section 33. He further pointed out that if the assessee does not resort to section 27, the Assistant Commissioner has no authority to entertain an appeal under section 30. All that the Assistant Commissioner is empowered to do is to consider whether the Income-tax Officer applied his mind to the relevant questions before making the assessment under section 23 (4). If he finds that the Income-tax Officer did not apply his mind, he has no power to entertain the appeal. As I understand the position when the Income-tax Officer acts under section 23 (4) and the assessee prefers an appeal to the Assistant Commissioner, all that the Assistant Commissioner has to do is to satisfy himself that the Income-tax Officer has carried out the necessary procedure which entitled him to take action under section 23 (4) and that he has not merely labelled his action as falling within the purview of that section. If the Assistant Commissioner finds that action has really and properly been taken under section 23 (4) he cannot entertain the appeal.

On behalf of the assessee Mr. Mehr Chand Mahajan has urged that the proviso to section 30 does not bar the Assistant Commissioner from examining the decision arrived at by the Income-tax Officer as to the liability of the assessee to assessment. Section 30 of the Income-tax Act runs as follows:—"Any assessee objecting to the amount or rate at which he is assessed under section 23 or section 27, or denying his liability to be assessed under this Act, or objecting to a refusal of an Income-tax Officer to make a fresh assessment under section 27; or to any order against him under sub-section (2) of section 25 or section 28,

made by an Income-tax Officer may appeal to the Assistant Commissioner against the assessment or against such refusal or order," and it is clear that the assessee has a right to appeal against the assessment made or against a refusal to make a fresh assessment, or against any order made under sub-clause (2) section 25 or section 28. The appeal is against the assessment and it has been specifically provided that where an assessment has been made under sub-section 4 of section 23, no appeal shall lie. In my judgment the interpretation of this section and the proviso has been correctly stated by the Commissioner in his reference. Section 30 gives an appeal against an assessment, or a refusal, or an order and provided the Income-tax Officer has carried out the provisions of sections 22 (4) and 23 (4) and then takes action under the latter section, the right to appeal against such an assessment has been taken away by the statute. It seems to me clear that the object of the Legislature was to compel assesseees to lay all the necessary materials before the Income-tax Officers in order to enable them to arrive at a correct decision. If an assessee fails to comply with the lawful orders of the Income-tax Officer, such an assessee is penalized by having his right to appeal taken away. The proviso distinctly lays down that no appeal shall lie in respect of an assessment made under sub-section (4) of section 23 and this to my mind clearly means that every matter that has to be decided before the assessment is arrived at is rendered unappealable.

I would answer the question referred accordingly.

CECIL FFORDE, J.:—I concur.

ZAFAR ALI, J.:—I concur.

(314) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

FULL BENCH.

Before Sir Shadi Lal, Kt., Chief Justice, Justice Sir Alan Broadway, Kt.,

Mr. Justice Zafar Ali, Mr. Justice Tek Chand and Mr. Justice Jai Lal.

(10th June, 1929).

Bhagat Jiwan Das and others

.. Assesseees.

v.

The Commissioner of Income-tax, Punjab and N. W.
Frontier Province

.. Referring Officer.

Income-tax Act (XI of 1922), Sec. 4 (1) and (2)—Assessee residing and carrying on business in British India—Goods purchased in British India and sold outside—Profits therefrom, if assessable.

Where the assessee residing and carrying on business in British India purchased goods in British India and sent them for sale to his shop outside British India.

HELD, that no portion of the profits derived from the sale outside British India, which was not received in or brought into British India was assessable, the mere purchase of goods having too remote a connection to justify the conclusion that a part of the profits should be held to have accrued in British India within the meaning of Sec. 4 (1) of the Income-tax Act.

Case [Civil Reference No. 18 of 1927], stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, Punjab and N. W. Frontier Province, for the opinion of the High Court.

CASE.

As a result of an application under section 66 (2) of the Income-tax Act, XI of 1922, the following question of law is referred to the High Court for decision:—Is a Hindu undivided family, which is resident in British India and does business of several kinds therein, liable to be assessed to British Indian Income-tax on any part of the profit accruing or arising to it from the sale outside British India of goods which it has purchased in British India? If so, on what part?

2. The facts of the case are briefly as follows:—The petitioners are a Hindu undivided family, which has for many years been resident at Haripur in the Hazara District of the N. W. F. Province, where business of various kinds, including a substantial money lending business, is carried on. An important business has also been carried on for many years at Srinagar outside British India. For the purpose of the latter, goods are purchased in British India and forwarded through Haripur and Rawalpindi for sale in Srinagar. When the family was assessed in 1924-25, the year in question, it was called upon by the Income-tax Officer, Hazara, to produce the accounts of the Srinagar business to enable him to determine the amount of profit liable to British Indian Income-tax. As the accounts were withheld, the Income-tax Officer was obliged to estimate the amount of this profit to the best of his judgment. This he did by applying a flat rate of profit, viz., 4 per cent. to the value of the goods purchased in British India and sold in Srinagar. Estimating the latter at 12 lakhs, he calculated that a sum of Rs. 48,000 had accrued or arisen by way of profit in British India. In applying a rate of 4 per cent. he took into consideration the fact that part of the profit earned on the purchase and sale of the goods, accrued or arose outside British India, i.e., where the goods were sold. Had they been sold, as well as purchased, in British India, a higher rate would have been applied. The assessment order was passed under section 23 (3). Actually it should have been passed under section 23 (4), as the accounts of the Srinagar business were deliberately withheld. Had it been passed under this sub-section, no appeal would have lain (*vide* proviso to section 30 (1)). As it was, however, an appeal was filed and entertained; and not only was it entertained, but the petitioners were allowed a further opportunity of producing the Srinagar accounts. The accounts, which were produced accordingly, showed that the value of the goods forwarded to Srinagar amounted not to 12 lakhs, as estimated by the Income-tax Officer, but to Rs. 8,26,886. The Assistant Commissioner, however, did not modify the assessment, as the accounts also showed that large sums had been remitted from Srinagar to British India by way of cash, Hundis and book transfer, and there was, in his opinion, reason to believe that a substantial part of these remittances was profit taxable under section 4 (2). He thought, therefore, that the petitioners had probably been under-assessed, *vide* his order dated 18-6-1925. The case then came up before the Acting Commissioner on review. As the Srinagar accounts showed that the value of the goods exported from British India had been over-estimated by the Income-tax Officer, assessable income under this head was reduced from Rs. 48,000 to 33,075, a figure calculated by applying the former rate of 4 per cent. to the value shown in the accounts (Rs. 8,26,886), *vide* order dated 9-1-1926.

3. In applying for review of the Income-tax Officer's assessment under section 33 of the Act, the petitioners contended that no part of this amount was taxable and requested that if the claim could not be conceded under section 33,

certain points might be referred to the High Court under section 66 (2). When the claim was rejected under section 33, the following point was substituted by the petitioners for the different points specified in the original application:—"Is the firm which purchased goods in British India for sale in the open market in Kashmir liable to be assessed to income-tax under Act XI of 1922". I took exception to the way the question was worded, as it omitted all reference to the fact that the petitioners' family is resident in British India. Enquiry showed that the fact was denied, and as the point was important, I remanded the case to the Assistant Commissioner for a definite finding, after full enquiry, as to whether or not the family was resident in British India. He was also directed to ascertain whether the family did commission, as well as money lending, business in British India. The latter was admitted but not the former, and though of minor importance, I thought it as well that the point should be definitely decided in case Your Lordships considered it relevant to the issue. After careful enquiry both points, which are both questions of fact, have been decided against the petitioners, *vide* my order of the 25th January 1927. The question now referred, specified in the opening paragraph, is the result of this order.

4. The case is governed by section 4 (1) of the Income-tax Act, which provides that the Act "shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing or arising, or received in British India." The question for decision is whether any part of the profit earned on the sale of goods purchased in, but sold outside, British India by a person resident and doing business of various kinds therein can be said to accrue or arise in British India irrespective of where it is actually received. In the business in question profit is the net result of three different operations—purchase, transport and sale. All three must be completed before any profit can be received, but not before profit begins to accrue. Accrual begins with the completion of the first operation and continues cumulatively till the goods are finally sold. This accords with the view expressed by Mr. Justice Mukerji in the case of *Rogers Pyatt Shellac and Co. v. Secretary of State for India*(1). In defining the difference between the words "accruing", "arising" and "is received" the learned judge remarked that the words "is received" are distinct from the words "accrues" and "arises", which merely indicate a right to receive, and explained that "they represent a stage anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate". And he added: "Income may accrue at one place, arise at another and be received at a third. Again it may accrue or arise in respect of or out of something situated at one place but accrue or arise to a person at a different place".

5. If these distinctions are correct—and logically they cannot, I think, be challenged—it follows that some part of the profit arising from the purchase and sale of the goods in question accrued and arose in British India where they were purchased and from which they were transported to Kashmir. This agrees not only with the view expressed in the case just quoted but also with that expressed by the learned Chief Justice of the High Court of Rangoon, who in the case *Steel Brothers and Co. Ltd. v. Commissioner of Income-tax, Burma*(2), observed as follows:—"We hold that the fact of the produce being sold in London and the money being received there does not prevent profits or gains accruing, or arising, or being deemed to accrue or arise in British India, from being taxable under the Indian Income-tax Act. We are also of opinion that no distinction, so far as liability to income-tax is concerned, can be drawn between

(1) 1 I. T. C. 363.

(2) 2 I. T. C. 119 at pages 136 & 138.

profits on produce, which has undergone some process of conversion or "working up" by the assessee in Burma and profits on produce purchased by the assessee in Burma and exported in the same form as when purchased". The learned Chief Justice observed further that "in determining whether any income, profits or gains arise or accrue, we must not be content to look only at the last stage of the accrual, but must take into consideration the previous stages as well".

6. I am of opinion, therefore, that part of the profit is taxable under section 4 (1) and that the first part of the question should be answered in the affirmative. As to the second part of the question, I am further of opinion that so much is taxable as may be deemed to have accrued or arisen from the operations of purchase and transport, so far as these operations have been carried on in British India. In the present case it is impossible to estimate this with mathematical accuracy, but the remarks of the learned Chief Justice in the Burma case referred to above may be quoted as affording a useful guide for the calculation. These are as follows;—"In arriving at the amount of profits liable to Indian income-tax, the Commissioner of Income-tax, in our opinion, should allow a reasonable commission agent's commission on the sale realization of the produce. So much of the profits as can reasonably be attributed to commission agent's commission should not be assessable." (1) In this case, had the goods been sold as well as purchased in British India, exact profit not being ascertainable from the accounts, a flat rate of $6\frac{1}{4}$ per cent. would probably have been applied, as this is the standard rate in such cases. In applying a rate of 4 per cent. the Department has made a substantial allowance for the fact that part of the profit arose outside British India.

7. In conclusion, I may note that the two cases cited above strongly support the view expressed in this reference. In both cases the question in issue was whether any part of the profit earned on goods exported for sale outside British India was taxable; and in both the question was decided in the affirmative. In one important respect, however, the cases are to be distinguished from the present. In neither was the assessee resident in British India. Owing to this, section 42 (1) of the Act had to be invoked to establish liability. In the present case, as the assessee both resides and carries on business in British India, this is unnecessary and liability is correspondingly clearer.

Dr. Moti Sagar, Mehr Chand Mahajan and Amar Nath Chona, for the Assesseees.

Jagan Nath Aggarwal and R. C. Soni, for the Crown.

JUDGMENT.

SHADI LAL, C. J.:—The question submitted to us may be stated in a few words. A person, who resides and carries on business in British India, purchases goods in British India and sends them for sale to his shop in Kashmir, a country outside British India. Is he liable to be assessed to income-tax under the Indian Income-tax Act, XI of 1922, in respect of any part of the profits derived from the sale of the goods; and if so, what part?

We may clear the ground by stating at the outset that we are not here concerned with the profits of the business which is carried on in British India, or with any part of the profits derived from the sale of the goods in the foreign country which have been received in or brought into British India. The profits of both these descriptions are certainly taxable in British India.

The answer to the question depends on the interpretation to be placed upon section 4, sub-section (1) of the statute, which, so far as it is material to

(1) 21. T. C. 119 at page 138.

the present discussion, is in the following terms:—"Save as hereinafter provided, this Act shall apply to all income, profits or gains * * * accruing or arising, or received in British India." *Ex concessio*, no part of the profits in this case has been received in British India; and the question, stripped of all irrelevant details, is thus narrowed down to the following issue: Whether a person residing in British India is liable to be assessed to income-tax under the Act on any part of the profits derived from the sale in a foreign country of the goods purchased by him in British India, when the profits have neither been received in, nor brought into, British India. It must be remembered that the Indian law bases the liability of a person to taxation on the place where the income (the word "income" is used in this judgment as a comprehensive term including not only what is strictly called income, but also profits and gains) accrues or arises or is received, but not on the place of his residence. If the place of accrual or arising or receipt is British India, the income is taxable, otherwise it is not, unless the income, though accruing or arising or received outside British India, is, by a fiction of law, deemed to have accrued or arisen or to have been received in British India. It is, however, conceded that the question before us is not affected by any such legal fiction, and, as stated above, no part of the profits was received in or brought into British India. We must, therefore, concentrate our attention upon the problem whether any part of the profits *accrued* or *arose* in British India.

The learned counsel on both sides are agreed that the expression "arising" as used in section 4, sub-section 1 is, to all intents and purposes, synonymous with the term "accruing". As observed by Mukerji, J., in *Rogers Pyatt Shellac & Co. v. Secretary of State for India*(1), "Perhaps the two words seem to denote the same idea or ideas very similar, and the difference only lies in this that one is more appropriate than the other, when applied to particular cases." The word "accrue" is not defined in the Act, but according to Murray's Oxford Dictionary it means "to arise or spring as a natural growth or result" and in Webster's Dictionary it has the meaning "to come to by way of increase"

Now, the profits of a transaction in the nature of a sale consist of the difference between the price received for the goods sold and the cost of procuring and selling them. In ordinary cases, profits can be ascertained only when the price is realised, because until realisation it cannot be said that the transaction will result in profits. But we are here concerned, not with the time when the profits accrue, but with the place at which they accrue. It is beyond dispute that the place, where the sale is effected and the price realised, is certainly the principal place, if not the place, of the accrual of profits.

Mr. Jagan Nath for the Commissioner of Income-tax, however, contends that a part of the profits accrued in British India where the goods were purchased, and he places his reliance upon the judgment of the Calcutta High Court in *Rogers Pyatt Shellac and Co. v. Secretary of State for India*(1). It was held in that case that a company incorporated in the United States of America and having its head office in New York and branch offices, agencies and factories in Calcutta, London and other places, which purchases goods in India for sale in the open market in America, or for another Company in America, and which has also a factory in the United Provinces where raw produce is bought locally and is worked up into a form suitable for export to America is not exempt from assessment to income-tax in British India. It will be observed that that case was decided with reference to section 38 sub-section (1) of the Income-tax Act, VII of 1918, which sub-section corresponded to section 42, sub-section (1) of the present Act, and enacted a special provision to the effect that in the case of

(1) 1 I. T. C. 363.

any person residing out of British India all profits or gains accruing or arising to such person, whether *directly* or *indirectly*, through or from *any business connection* in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed for all purposes of the Act the assessee in respect of such income-tax.

The decision of the case proceeded upon the fiction introduced by the statute under which income, though *actually* accruing out of British India, is deemed to accrue in British India. Far from lending any support to the contention of the learned counsel, the judgment contains some observations which go against him. As stated by Chatterjea, J., no part of the Company's income actually accrued, arose or was received in British India, but under section 31, sub-section (1) it should be deemed by a fiction of law to have accrued in this country.

The judgment of the Rangoon High Court in *Steel Bros. Co. Ltd., v. Commissioner of Income-tax, Burma*(1), is also founded upon the same fiction. In that case the assessee was a limited company incorporated under the English law, and was admittedly non-resident in British India, having its headquarters in London. It carried on various large business undertakings in Burma, especially in connection with rice, timber and cotton. It also had numerous rice mills, saw mills, cotton ginning mills and vegetable oil mills in Burma, where commodities or raw material were "worked up into forms suitable for use" and shipped to the United Kingdom. It also exported from Burma raw commodities in the same form as purchased. The learned Judges decided that the profits or gains must be deemed under section 42, sub-section (1) of the Indian Income-tax Act, XI of 1922, to have accrued or arisen in British India, and were therefore, taxable under the Indian law. It was a case in which the profits accrued to a non-resident through or from a business connection or property in British India; and the assessee was clearly liable under the special provision referred to above on the ground that the profits should be deemed to have accrued in British India irrespective of the fact whether they did, or did not, *actually* accrue there. It is true that there are observations in the judgment which, if divorced from the context, can support the view that a part of the profits may be attributed to the mere fact of the purchase of the goods in British India, but, as the case clearly came within the language of section 42, sub-section (1), those observations cannot but be treated as *obiter dicta*. Moreover, as pointed out by Lord Halsbury in *Quinn v. Leathem*(2), "every judgment must be read as applicable to the particular facts proved, or assumed to be proved, since the generality of the expressions which may be found there are not intended to be expositions of the whole law, but governed and qualified by the particular facts of the case in which such expressions are to be found."

Mr. Mehr Chand Mahajan for the assessee invites our attention to two judgments of the Madras High Court in order to establish the proposition that no part of the profits can be held to accrue at that place where the goods are merely purchased. In *Board of Revenue v. Ramanadhan Chetty*(3), the rule was laid down that a person residing in British India, who is the proprietor of a money lending business carried on for him outside British India by agents resident there and keeps himself acquainted with the progress of the business and issues general instructions to his agents carrying on the business, is not assessable to Indian income-tax if the income from such business is not

(1) 2. I. T. C. 119.

(2) (1901) A. C. 495.

(3) 1 I. T. C. 37.

remitted to British India. This judgment is clearly distinguishable and cannot be of any assistance in the present case. But the decision in *The Secretary, Board of Revenue, Madras v. The Madras Export Co.*(1), has an important bearing upon the question before us. In that case a firm situated in Paris bought raw skins in Madras through an agent who exported them to Paris where they were sold on profits by the firm. A Division Bench of the Madras High Court held that the profits accrued wholly in France and were not, therefore, taxable in British India. The principle upon which that judgment proceeds, is applicable to the present case. In that case, as here, goods were purchased in British India, and exported to a foreign country where they were sold and the sale resulted in profits. It is true that in the Madras case the person entitled to the profits was residing in a foreign country while in the present case the assessee resides in British India. But this difference is wholly immaterial, because, as stated above, the Indian law makes the place of the accrual of the income, and not the place of the residence, as the test of liability. If, as held in the Madras case, income accrued wholly outside British India, and no part of it can be regarded as having accrued in British India on account of the purchase of the goods in British India, there is no reason why a different rule should govern the present case.

It is necessary to point out at this stage that this judgment, in so far as it decided that section 33, sub-section (1) of the Indian Income-tax Act of 1918 was not a charging section, but merely a machinery section, (that is to say, a section which provides a method of carrying out the charge imposed by some other section), has been dissented from by the Calcutta High Court in *Rogers Pyatt Shellac & Co. v. Secretary of State for India*(2), and by the Rangoon High Court in *The Commissioner of Income-tax, Burma v. Messrs. Steel Brothers & Co. Ltd.*(3). In both these cases it was ruled that any income accruing or arising to a non-resident through or from any business connection or property in British India should be deemed to be income accruing or arising within British India; and that it was immaterial whether the income did, or did not, actually accrue or arise in British India. But, as observed above, these judgments proceed upon the special rule enacted by the statute by which income, actually accruing at one place is deemed in certain circumstances to accrue at another place. It cannot, therefore, be reasonably argued that they enunciate any rule different from that laid down by the Madras High Court that the profits actually accrue or arise at the place where the goods are sold, and not at the place where they are merely purchased for export.

It would appear from the judgment in *Rogers Pyatt Shellac & Co. v. Secretary of State for India*(2), that if the charging section had not been enlarged by section 33 sub-section (1) of Act VII of 1918, (section 41, sub-section (1) of the present Act), the learned Judges would have held that the company in that case was not liable to pay income-tax in this country. It is to be observed that while the statute has enacted a special rule making a non-resident having business connection or property in British India liable to Indian income-tax in respect of the income accruing outside the territorial limits of British India, there is no corresponding provision imposing a similar liability on a resident who derives income from the sale in a foreign country of the goods purchased by him in British India. We cannot extend the scope of the statute by analogy or place upon it what is called a beneficial or equitable construction in order to prevent a real or supposed anomaly. As observed by Lord Cairns in

(1) 11 T. C. 194.

(2) 11 T. C. 363.

(3) 21 T. C. 119.

Partington v. Attorney-General(1) "As I understand the principle of all fiscal legislation, it is this: if the person sought to be taxed comes within the letter of the law, he must be taxed, however, great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however, apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible, in any statute what is called an equitable construction, certainly such a construction is not admissible in a taxing statute where you should simply adhere to the words of the statute."

The same rule of construction has been enunciated by Lord Buckmaster in the recent case of *Greenwood v. Smidth & Co.*(2), in the following words:—"It is important to remember the rule which the Courts ought to obey that when it is desired to impose a new burden by way of taxation it is essential that the intention should be stated in plain terms. The Courts cannot assent to the view that if a section in a taxing statute is of doubtful and ambiguous meaning it is possible out of that ambiguity to extract a new and added obligation not formerly cast upon the tax-payer". Not only is there no provision indentifying the place of the accrual of income with the place where the goods are purchased, but there is some indication in the statute to the contrary. Take the case of a person who purchases goods in a foreign country* and sends them to British India for sale. Section 42, sub-section (3) lays down that the profits shall be deemed to have accrued and arisen and to have been received in British India. This sub-section shows that where goods are purchased in a foreign country and sold in British India, the Indian law regards by a legal fiction or otherwise the place of the sale, and not the place of the purchase, as the place of the accrual of profits.

We have been referred by the learned counsel on both sides to some decisions of the English Courts on the Income-tax Acts of England, but they cannot furnish any guidance in the present case because the scheme and the phraseology of the English Acts are wholly different from those of the Indian statute. I must, however, examine the judgment of the Privy Council in *The Commissioners of Taxation v. Kirk*(3), which is claimed by Mr. Jagan Nath as a direct authority in support of his contention. In that case, the assessee was a company incorporated in the colony of Victoria and had its head office with a Board of Directors at Melbourne in that colony. The Company carried on the business of mining on lands held on lease from the Crown in the Colony of New South Wales where it had an office and a manager of the mines. The ore extracted from the mines in New South Wales was treated by the Company's plant and converted into a merchantable product in that colony, but the sales of the products were made and the purchase money was received either in London or in Victoria. The company made profits from these business operations, and the question arose whether any part of the profits was assessable to taxation under the New South Wales Land and Income-tax Assessment Act of 1895. Now, section 15 of that statute provided that income-tax was payable in respect of the annual amount of all incomes** (1), arising or accruing to any person wheresoever residing from any profession, trade * * * * * carried on in New South Wales; (3) derived from lands of the Crown held under lease or license issued by or on behalf of the Crown; (4) arising or accruing to any person wheresoever residing * * * * * from any other source whatsoever in New South Wales not included in the preceding sub-sections.

Their Lordships of the Privy Council held that the case came under sub-section (3) in so far as the income derived from the extraction of the ore from the

(1) (1869) L. R. 4 H. L. 120.

(3) (1900) A. C. 588.

(2) 8 Tax Cas. 193.

Crown lands was concerned, and also under sub-section (4) because of the conversion of the crude ore into a merchantable product which is a manufacturing process, and which, if not within the meaning of "trade" in sub-section (1), was certainly included in the words "any other source whatever" in sub-section (4). It is clear that both the processes referred to in the judgment came within the ambit of section 15, and the income derived therefrom was accordingly held to be taxable in the colony of New South Wales.

Considering that the judgment of the Privy Council deals with a case in which the business was admittedly carried on in New South Wales, I do not think that it can be cited as an authority for the proposition that the mere purchase of goods in a country for the purpose of enabling a person to trade in another country makes him liable to taxation in the former country on the ground that a part of the profits should be treated as having accrued there. The judgment in *Sully v. Attorney-General*(1), makes it absolutely clear that the mere purchase of goods in a country does not amount to an exercise of trade in that country. Though the test of liability under the English Act is the exercise of trade in the United Kingdom, the following observations of Cockburn, C.J., are nevertheless pertinent here:—"Wherever a merchant is established, in the course of his operations his dealings must extend over various places; he buys in one place and sells in another. But he has one principal place in which he may be said to trade, viz., where his profits come home to him. That is where he exercises his trade. It would be very inconvenient if this were otherwise. If a man were liable to income-tax in every country in which his agents are established, it would lead to great injustice. The argument for the Crown must be carried to this extent, that merely buying goods in this country is a trade exercised here so as to subject the purchaser of the goods to income-tax

* * * * *

It would be most impolitic thus to tax those who come here as customers. The subjects of a foreign state, not resident here, cannot be made amenable to our laws. How then are their profits to be made amenable to the fiscal law? Simply by the provision that whosoever carried on the business and received the profits here shall be assessed. But in the present case no profits are received by the firm, or exist in this country.

The learned counsel for the Commissioner of Income-tax argues that the purchase of goods is one of the several processes the combination of which results in profits; and that a part of the profits should, therefore, be attributed to that process. It is, however, conceded by the learned counsel that, if the assessee did not himself purchase the goods in British India, but asked his agent in the foreign country to order them from a firm in British India, no part of the profits could be assigned to any process performed in British India, and that the whole of the profits would, in that case, be exempt from taxation under the Indian law. On principle there is little or no difference between the two cases. The same remarks would apply to the case of a person who, instead of buying goods in the market, exported his own goods, e.g., the raw produce of his own land, to a foreign country for sale by his agent there. If the mere purchase of goods in British India would have the effect of making British India as the place of the accrual of a part of the profits, the same result could, by a parity of reasoning be ascribed to the passage of goods through British India in the course of their transit, say, from one Native State where they are purchased to another Native State where they are sold and result in profits. I do not, however, think that this circumstance alone would render a part of the profits taxable in British India.

The question, upon which we have to pronounce our opinion is not free from difficulty; but after a careful examination of the arguments urged on both

(1) 2 Tax. Cas 149.

sides I have reached the conclusion that the mere purchase of goods in British India has too remote a connection to justify the conclusion that a part of the profits should be held to have accrued in this country. I would, therefore, answer the question by stating that no part of the profits realised by the assessee by the sale of the goods in the foreign country, is taxable under the Income-tax Act of 1922.

BROADWAY, J.:—I concur.

ZAFAR ALI, J.:—So I do.

TEK CHAND, J.:—I concur.

JAI LAL, J.:—I concur.

(315) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Brown and
Mr. Justice Chari.*

(13th June, 1929).

The Burma Corporation, Ltd.

.. Assessee.*

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

*Income-tax Act (XI of 1922), Sec. 10 (2) (ix)—Burma Corporation, Ltd.
—Staff Provident Fund—Execution of a Trust deed and creation of a fund
therefor—Corporation's contributions to the Provident Fund—When deductible
—Test is payment and not crediting in account.*

The Burma Corporation, Ltd., started a Staff Provident Fund in 1921 under the control of their Directors wherein three accounts were kept, A account consisting of a certain percentage of the employees' salaries, B account being the Corporation's bonus equal to the employees' contribution and C account, another bonus proportionate to the dividend and salaries of the employees. Under the rules of the Provident Fund a dismissed employee was entitled only to the amount to his credit in A account and accrued interest thereon and an employee acquired no right in or to the moneys to his credit in B and C accounts which remained the property of the Corporation.

In 1926 the Corporation executed a trust deed in respect of this Provident Fund, by which the Corporation vested in the Trustees by transfer of Government securities a fund sufficient to cover the Corporation's liability in respect of this Provident Fund and undertook to add to this Fund from time to time so as to cover the liabilities outstanding. The trust deed provided inter alia that the Trustees were to apply all monies in their hands in satisfaction of the claims arising under the rules and pay the balance to the Corporation, to call upon the Corporation, in case any securities in their hands fell short of the Corporation's liability, to supply that deficiency either by cash payment or by furnishing further security, while there was no obligation on the Corporation to make periodical payments of any sums to the Trustees.

On an assessment to income-tax for the year 1928-1929, the Corporation claimed a deduction of their contributions to the Provident Fund as an amount when credited to the Trustees during the account year ending June 1927.

* (1929) 7 Rang. 608 ; A. I. R. (1929) Rang. 193.

HELD, that the Corporation would be entitled to deduct the actual cash payments made to the Trustees either for the purpose of meeting liabilities of the retiring or deceased members, or for the purpose of supplying any deficiency in the Fund as contemplated by the trust deed and not the sums merely credited in their accounts.

The real test is whether the Corporation actually paid the money to the Trustees and lost all proprietary rights and powers over the sums so paid, and the mere fact that in some cases the Corporation might be entitled to get back a part of the amount paid made no difference in the legal position.

Case [Civil Reference No. 5 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

CASE.

I have the honour to refer to the High Court under section 66 (2) of the Indian Income-tax Act, 1922, a question of law arising out of the order of the Commissioner on the appeal of the Burma Corporation, Limited, (hereafter called the Company) against its assessment for 1928-29.

2. In the Company's assessment for the year 1928-29 there was included a sum of Rs. 5,40,599 which was the Company's contribution during the accounting year to its Staff Provident Fund. The Company claimed that this sum was allowable expenditure incurred for the purpose of earning the profits, but the assessing officer (in this case an Assistant Commissioner) did not allow it and his decision was upheld by the Commissioner on appeal. The Company being dissatisfied with this decision has asked me to make this reference.

3. The Company's Staff Provident Fund came into effect as from the 31st December 1921 and is governed by certain Rules and Regulations a copy of which is annexed and marked X.* On the 3rd November 1926 a trust deed was executed by which the Company vested in trustees, subject to certain trusts, a fund sufficient to cover the Company's liability under the rules aforesaid and undertook to add to this fund from time to time so as to cover the liability outstanding. A copy of this Trust Deed is annexed and marked Y.*

4. The following is a summary of the relevant provisions of the Rules and the Trust Deed:—(a) The Provident Fund (which must be distinguished from the Provident Trust Fund), consists of contributions by each member to his account called "A" account, contributions by the Company to his accounts called "B" and "C" accounts and interest at 5 per cent. allowed by the Company on all three accounts. (b) The Fund is controlled by the Directors of the Company whose decision is final. (c) The Directors may expel any member from the Fund and completely discharge its liability to him by paying him his "A" account with interest: but this power will only be exercised for reasons which in the view of the management require such action to be taken. (d) The amounts at the credit of a member's "A", "B" and "C" accounts may not be withdrawn until he leaves the Company's service, and even then the Directors can withhold portion of the "B" and "C" accounts if the member has not served for the required period. (e) If a member is dismissed for misconduct or leaves without permission he shall be paid only his "A" account with interest. (f) In addition to the foregoing provisions it is definitely stated that "no rights in or to monies at the credit of a member's 'B' or 'C' account shall vest in such member." (g) The Company has a first lien on the amounts standing to a member's credit

in the Fund in respect of loss, damage, etc., caused to the Company by his misconduct, negligence, etc. (h) The Directors may wind up the Fund on giving six month's notice to the members. (i) The functions of the Trustees may be summarised as follows:—They are to receive from the Company and hold a fund sufficient to cover the Company's liability under the Provident Fund Rules. The amount payable to this Fund by the Company is computed by and certified to by the auditors of the Company. The Trustees must obey the directions of the Company in regard to investing the Fund or realizing investments belonging to the Fund. Any excess over the Company's liability is to be held by the Trustees on trust for the Company and the Company may recover the excess from them. They must pay the income of the Fund to the Company. Subject to the foregoing the Trustees hold the Fund for the members of the Provident Fund and in the case of a winding up, they must first satisfy all claims arising under the rules and then pay the entire balance to the Company. If the Trustees cannot at any time lawfully apply the fund and its income to the purposes specified, the trusts shall determine and the fund shall be made over to the Company. (k) All claims of members against the Fund shall in the first instance be settled and paid by the Company.

5. The Company's contribution to the Provident Fund during the accounting year ending 30th June 1927 was Rs. 5,40,599. It is by no means clear that this amount representing contributions for the year in question was actually paid out to the Trustees during the year but in order not to complicate matters, I take it to be the fact that this sum of Rs. 5,40,599 being the Company's contributions to the Provident Fund was paid over over to the Trustees during the accounting year.

6. The question of law which I am asked to refer is as follows:—“Are the contributions of the Burma Corporation, Limited, to the Company's Staff Provident Fund assessable to income-tax and super-tax? As noted in paragraph 4 (a) above the Provident Fund must be distinguished from the Provident Trust Fund, and, as I understand the Company's case, it is based on the establishment of the Trust Fund. The question therefore refers to contributions to the Provident Trust Fund and I discuss it on that footing. But if the Company should contend that, irrespective of the amounts paid to the Trustees, all contributions credited in the Provident Fund books to its employees are allowable, I submit that there is no substance in this contention since the contributions in question, if not paid to the Trustees, remain in the Company's possession and do not leave it even temporarily.

7. It is admitted by this Department that contributions to Provident Funds constituted under irrevocable trusts are allowable expenditure under section 10 (2) (ix) of the Income-tax Act. Where there is an irrevocable trust it is clear that the employer has finally parted with his contributions. But in this case there is no question of irrevocable payments since there are many contingencies depending on the will of the Company in which the Company can reduce its liability and recover its contributions.

8. My opinion on the question referred therefore is that payments to the Trustees are not “expenditure incurred” within the meaning of section 10 (2) (ix) since the Company has not paid out finally or parted irrevocably with these sums. I refer to *Nedungadi Bank, Limited v. Commissioner of Income-tax, Madras*(1), in which a similar question was decided. It appears to me clear that taking the Rules and the Trust Deed as they are, expenditure allowable under section 10 (2) (ix) is incurred by the Company only when payments are

finally made to members. Such payments are in fact being allowed in the Company's assessments.

Clifton, for the Assessee.

Government Advocate, for the Crown.

JUDGMENT.

This is a reference by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act. The circumstances under which the reference is made are that the Burma Corporation, Ltd., has started a Provident Fund for their employees. By the terms of the rules of the Provident Fund, which is controlled by the Directors of the Corporation, it is provided that, in respect of employees, who are divided into two classes, an amount equal to $8\frac{1}{3}$ per cent. of the salary in the case of Class I and 5 per cent. in the case of Class II should be debited monthly from the salary of the employee. This amount was credited to an account which is called the "A" account and the Corporation agreed to pay interest at the rate of 5 per cent. per annum on the amount so credited which was added to the principal once every six months. The Corporation contributed a bonus equal to the amount deducted from his salary and this amount was credited in a separate account called the "B" account and interest was added to this sum in the same manner as in respect of the sums under the "A" account. There was also a "C" account which was another bonus credited to the employee proportioned on the dividend paid by the Corporation and the amount of the salary of the employee.

It will thus be seen that while the money in "A" account was the employee's own money, the moneys in the "B" and "C" accounts were the contributions made by the Corporation.

Rule 13 of the Provident Fund Rules provided that if any member were dismissed, he was entitled only to the amount standing to his credit in "A" account and the interest which had accrued thereon and that all the moneys credited to his "B" and "C" accounts should remain the property of the Corporation; and Rule 14 specifically provided that no member *acquired any right* in or to the moneys standing to his credit in "B" and "C" accounts.

In November 1926 the Corporation started a Trust in respect of the Provident Fund, to the terms of which we shall refer more in detail later. On the 31st December 1925 the liability of the Corporation in respect of the Provident Fund amounts payable to the members amounted to Rs. 12,58,782-4-11. By the Trust Deed three persons mentioned therein were made Trustees and Government securities of the nominal value of Rs. 14,25,000 and the actual value at market rate of Rs. 12,61,125 were made over to them. It will be seen that no money was entrusted to the Trustees, but the transfer of the securities to the Trustees may be considered as a payment of the equivalent of money to them, or the money may be considered as having been actually advanced to them in cash and taken back by the Corporation as a loan on the security of the Government promissory notes.

The point for consideration on this reference is whether the contributions of the Burma Corporation to the Provident Fund for the year ending with June 1927 are assessable to income-tax and super-tax. The learned Commissioner in his reference states—a statement with which we are in entire agreement—that it is not clear whether the contributions for the year in question were actually paid to the trustees, but in order not to complicate matters he is willing to assume that the sum representing the contributions of the Company was actually paid over to the Trustees. In making this concession, the Commissioner practi-

ally concedes the whole case, because in our opinion, the non-liability of the Corporation to assessment or otherwise depends entirely on whether the Corporation has or has not parted with the money. Fortunately the form of the question enables us to answer it in such a way as to enable the Commissioner to make enquiries on this point and adopt the course consonant with the result of his enquiries.

The contention of the Corporation seems to be that when the amounts are credited to the Trustees, it is entitled to a deduction of this amount from the amount for which it is assessable to income-tax and super-tax. The Commissioner admits that the contributions to the Provident Fund under an irrevocable trust are allowable expenditure under section 10 (2) (ix) of the Income-tax Act, but he contends that this section would apply only when there is an irrevocable trust and when the employer has finally parted with his contributions. He is of opinion, on a construction of the trust deed, that there is no question of any irrevocable trust since there are many contingencies dependent on the will of the Corporation on the happening of any of which the Corporation can reduce their liability and recover their contribution. The Corporation, on the other hand, contends that the trust is none the less an irrevocable trust, simply because in certain contingencies the Corporation will be able to get back its contributions. In this contention, the learned advocate for the Corporation is in the right. Even without any express provision in the trust deed where the purposes for which the trust is created have been fulfilled or fail there will be a resulting trust in favour of the author of the trust of any undisposed off amount in the hands of the Trustees. This does not, however, dispose of the matter because the real point is a different one.

We shall now refer to a case which has been cited before us. In the *British Insulated and Helsby Cables, Limited v. Atherton*(1), the facts were somewhat similar to the facts of the present case. There a pension fund was created and was constituted by a trust deed. The company contributed a sum of £31,784 to form the nucleus of the fund and to provide for payment in respect of the past years of service of the employees. It was practically admitted in that case that this money must be deemed to have been wholly and exclusively laid out for the purpose of the trade and therefore deductible under the provisions of the English Income-tax Act corresponding to those in our own Act; but it was contended that it was in the nature of a capital expenditure, and therefore the company was not entitled to any deduction. The point actually decided was only in respect of the sum of £31,784, it being conceded that yearly payments by the company equivalent to the deductions out of the salary of the members would be entitled to be deducted from the current year's income. It is not, for the purposes of the case before us, necessary to refer to more in this judgment than a significant passage in the judgment of Lord Atkinson.

At page 219, of the report he gives a summary of the terms of the trust deed created by the British Insulated and Helsby Cables. After setting out the important provisions of the deed he concludes as follows:—"The trust deed contains many other provisions supporting the conclusion that the company have once and for all parted with all proprietary rights in and all powers over this donation of £31,784." This ruling was relied upon by the learned advocate for the Corporation as an authority which shows that payment to the trustees of a fund would enable a company to claim deduction of the amount so paid, in the same way as a payment to the employee direct, but the concluding passage cited above clearly shows that the real test is whether the Corporation actually pays the money to the Trustees and loses all its proprietary right in and all powers over the sums so paid. The mere fact that in some cases it may be

(1) 10 Tax Cas 155 ; (1926) A. C. 205.

entitled to get back a portion of the amount paid out makes no difference in the legal position.

Turning now to the trust deed before us: the powers of the Trustees are contained in clause 2 of the Trust Deed. They are six in number. Clause (a) makes it obligatory on the Trustees to realise any portion of the Provident Trust Fund represented by any security if the Corporation desire it to be so realised; Clause (b) makes it obligatory on the Trustees to reinvest the amount so realised in such other securities as the Corporation may direct; Clause (c) provides that whatever sum there may be in the hands of the Trustees in excess of the liability of the Corporation shall be held by them in trust for the Corporation who may from time to time recover such excess; Clause (d), which is the most important clause, provides that the Trustees shall stand possessed of the corpus and income of the Provident Trust Fund on trust for the members for the time being of the Provident Fund and upon a winding up of the Provident Fund or of the undertaking of the Corporation, upon trust to apply all moneys in their hands in satisfaction of the claim arising under the rules and secondly in payment of the entire balance to the Corporation; Clause (e) provides that the income of the Provident Fund, if any, is subject to the trusts declared by sub-paragraph (d) payable to the Corporation; Clause (f) provides that if the Trustees shall at any time be unable lawfully to apply the Provident Trust Fund and the income thereof or any part of such fund, then the trusts hereby created shall determine and the Provident Fund and the income thereof shall forthwith be made over to the Corporation. Paragraph 3 provides that whenever on any of the accounting days it shall be ascertained that owing to market depreciation of the securities the corpus of the Provident Fund is less than the amount of the liability of the Corporation, then the Corporation will pay to the Trustees a further such sum as will be necessary to make good the deficiency in cash or some security or securities authorised by the law of British India for the investment of Trust Funds or partly by one or partly by the other.

The noticeable feature of this trust deed is that there is no obligation on the Corporation to make periodical payments of any sum whatever to the Trustees. The deductions out of the salary carried in "A" account is not paid to them, nor are the contributions of the Corporation carried in the "B" and "C" accounts.

It is true that the Trustees have the power whenever any security they may have in their hands is short of the liability of the Corporation, to call on the Corporation to supply that deficiency either by cash payment or by furnishing further security, but till the Trustees think fit to act on this clause, there is no obligation on the Corporation to make any payment. The credit in the accounts in favour of the employees or the Trustees makes no difference. The object of the Trust, as far as one can see, is not to create a fund in cash vested in the Trustees over which the Corporation have lost all control and proprietary rights, but to create a body which would be able to secure for the members satisfaction of the liability of the Corporation. As is seen from the remarks in Lord Atkinson's judgment, the real ground on which the Corporation can claim exemption from payment of income-tax is that they have actually parted with the money. The transfer of a book debt, even assuming that as from the date of the Trust Deed the Trustees are the persons credited in the "A", "B" and "C" accounts on behalf of the members, does not mean that the Corporation have either parted with the money or lost control over it. In our opinion therefore, the Corporation will be entitled to deduct from the amount assessable to income-tax the actual cash payments made to the Trustees either for the purpose of meeting liabilities of the retiring or deceased members as they arise or for the purpose of supplying any deficiency as contemplated by paragraph 3 of

the Trust Deed. They are not entitled to any deduction in respect of the sums merely carried in the account, as the mere creation of a book liability whether in favour of the employees or Trustees is not equivalent to a payment.

The difference between the Corporation and the Commissioner was merely as to the point of time when the Corporation becomes entitled to a deduction for these amounts. The Commissioner, in view of the provisions of the Trust Deed, was of opinion that the Corporation is entitled to a deduction only when the amount payable to the employee has been paid to him. In this, he is wrong because the Corporation, notwithstanding the provisions of the deed, would be entitled to deduction if it has actually paid the amount of its yearly contributions to the Trustees in such a way as to have lost their proprietary right in and control over them. The Trustees will hold the money primarily as Trustees for the employees, though in certain cases, a portion of the money may become repayable to the Corporation. When the moneys are so repaid they will be an addition to the income of that year and as such assessable. The contention of the Corporation is not quite clear. If the position of the learned advocate of the Corporation is that by a mere credit in favour of the Trustees instead of the employees, and the creation of a liability to the Trustees for the payment of these contributions, the Company can deduct the amounts so credited from the assessable sum, notwithstanding they have full control over and unlimited use of the money represented by the credit, we cannot accept his contention.

Our answer to the reference therefore is that the contributions of the Burma Corporation, Ltd., to its Staff Provident Fund are not assessable to income-tax and super-tax, if the money had actually been paid to the Trustees and the Corporation has lost the control over and the use of the money.

In these circumstances we make no order as to costs.

(316) IN THE HIGH COURT OF JUDICATURE AT FORT WILLIAM IN BENGAL.

*Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose and
Mr. Justice Buckland.*

(4th July, 1929).

Ganga Sagar Ananda Mohan Shaha

.. Assessee.*

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Indian Income-tax Act, (XI of 1922),—Dayabagha Hindu undivided family—Business started by four brothers—Descendants carrying on business with separate mess and separate businesses—Business accounts unadjusted—Joint family, if disrupted.

The assessees, sons and grandsons of 4 brothers who as an undivided Hindu Dayabagha family started a business three generations ago, were living and messing separately with separate house properties and businesses of their own and were drawing monies from the business for their mess and other expenses such as marriage, construction of houses, etc., debited to the separate accounts of the branches of the family. In the accounts of the business there was no capital credit either in the name of the family, or its branches, the accounts in the names of the branches remaining unadjusted showing the periodical drawings resulting in a large debit with no credit.

HELD, that the original undivided Hindu family had ceased to exist and that the assesseees were not entitled to be assessed as a Hindu undivided family.

Case stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Bengal, in compliance with the order of the High Court, dated 13th December, 1927.

CASE.

With reference to the order of the Hon'ble High Court under section 66 (3) of the Indian Income-tax Act contained in their Judgment delivered on the 13th December 1927, asking me to state the question whether or not the assesseees are entitled to be treated for income-tax purposes as a Hindu undivided family for their opinion, I have the honour to state that I caused further enquiries to be made the results of which have been incorporated in the facts of the case given below.

2. The business was originally started by four brothers Gangasagar, Ananda Mohan, Broja Mohan and Hari Mohan Shaha, who were members of a Hindu undivided family. These brothers died long ago and their heirs are now the proprietors of the business. These heirs are now living in four separate houses and consequently in separate mess for the last 15 or 16 years. The heirs of each of the four brothers named above are living in the same house and in the same mess. The cost of constructing these separate dwelling houses for the heirs of the four original proprietors is admitted to have been debited to the accounts of the heirs of the four original proprietors respectively. The cost of messing is admittedly met separately by the heirs of the four original proprietors out of their own funds, which include sums drawn from the business in question according to their requirements. These drawings from the business are likewise debited to the separate accounts of the heirs of each of the four original proprietors, who for the sake of convenience may be known as separate branches of the family. The expenses of marriages and education of children are defrayed in the same way by the different branches separately.

3. No family idol is maintained by any of the separate branches of the family, and no *Pujahs* of any kind are performed by any of these branches. No question of joint worship, therefore, arises.

4. The account books of the business do not show any capital account either in the name of the alleged undivided Hindu family or in the names of the separate branches of the family, but there are accounts in the names of the heirs of the four original proprietors which practically show only their drawings from the business. In these accounts the credit side shows either *nil* or some paltry sum, while the debit side in every case shows a large sum.

5. The share of each of the four branches is said to be one-fourth, but, as the accounts of the business have never been adjusted, the accounts in the names of the heirs of the four original proprietors have not also been adjusted so far. The balances are however carried forward from year to year, pointing to the conclusion that when the accounts are finally adjusted the drawings of the heirs of the four original proprietors will be taken into consideration, and the profits or losses of the business will be allocated to each branch accordingly.

6. It is significant that the four branches have got separate businesses of their own, the incomes from which are being separately assessed to income-tax along with the other incomes of the respective branches.

7. These are all the facts that could be gathered in this case. On being asked to produce evidence in support of their claim to be treated as a Hindu

undivided family, the assessee simply filed an affidavit sworn by one of the proprietors to the effect that the proprietors of the business all belong to one undivided Hindu family, and that although there are separate messing arrangements for the sake of convenience, the family having become a very big one, the expenses of all the proprietors are met from the funds of the business. As accounts had already been examined the representative, who appeared, stated that the assessee had no other evidence to produce.

8. There are a few other facts which the assessee has tried to explain away on the plea of ignorance of law. But they are again mentioned below for the sake of easy reference as they appear to have some force when read with the facts stated above.

9. The business has throughout been assessed as an unregistered firm, as the assessee never claimed to be assessed as a Hindu undivided family. The four separate branches have been filing separate returns of their own income, and have been assessed separately since the year 1923-24. In calculating the proper rate of tax the partnership income of each of the branches from the main firm has been taken into account every year without any objection. In the years 1923-24 and 1925-26 the business in question was assessed to super-tax. The statutory allowance given was Rs. 50,000 and not Rs. 75,000 and no objection was raised. It was not till the appeal stage in the assessment with which we are concerned, that the assessee claimed to be assessed as a Hindu undivided family.

10. On the 25th July 1927, the assessee, in compliance with a notice under section 38 gave a list of "*Angshidars*" which naturally means "partners" in which each separate branch of the family was shown to be the proprietor of one-fourth share in the business in question. It may be mentioned that under section 38 the Income-tax Officer may require a firm or a Hindu undivided family to furnish the Income-tax Officer with a return of the members of the firm or of the manager or adult male members of the family, as the case may be, and of their addresses. The return filed shows not only the names of the male partners, but also of female and minor partners, so evidently it was not intended to be a return of the members of a Hindu undivided family.

11. I have said before that the four branches are separately assessed. In each of these assessments one-fourth share of the profits of the business in question together with the income of the separate business of the particular branch of the family, and the *bona fide* annual value of the house properties belonging to that branch are taken into account. This shows clearly that the assessee admitted separate ownership of business and properties of the four branches. It is not clear how the separate businesses were started, but the inference is that this was done with capital drawn from the business in question and debited to the accounts of the respective branches. The house properties were admittedly constructed with money from the business in question debited to the account of the respective branches. Had the four branches formed one and the same Hindu undivided family, the house properties should have belonged to that undivided Hindu family, and no debits should have been raised against the heirs of the four original proprietors.

12. The admission of this separate ownership of business and properties seems to be a strong proof of the division of the original undivided Hindu family into four undivided Hindu families, and in consideration of this and of the other facts mentioned above I am of opinion that the business in question is not that of a Hindu undivided family, but that of an unregistered firm.

N. C. Bysack, G. C. Das and Satyendra Ghose, for the Assessee.
S. N. Sirkar and N. N. Bose, for the Crown.

JUDGMENT.

GHOSE, J.:—In this matter the Commissioner of Income-tax, Bengal, was directed by an order made by this Court* on the 13th December, 1927, to state a case for the opinion of the Court, whether or not the assesseees were entitled to be treated for income-tax purposes as a Hindu undivided family. The Commissioner of Income-tax has accordingly stated a case for the opinion of the Court.

The facts found by the Commissioner of Income-tax are as follows: It appears that four brothers governed by the Dayabhaga School of Hindu law named Ganga Sagar, Ananda Mohan, Brojo Mohan and Hari Mohan Shaha, who were members of a Hindu undivided family started a business many many years ago. These four brothers are dead and their sons and grandsons are now carrying on the business. The places of business at present are, among others, Calcutta, Dacca and Backerganj, the head office being at Dacca. For many years past, the heirs of the said four brothers have drawn monies separately from the business, the monies debited to the separate accounts of the heirs of the said four brothers in the books of the business. These heirs separated in mess about 15 or 16 years ago and have been living in four separate houses (the heirs of each of the four brothers living in the same house and the same mess), the cost of constructing which was drawn from the business and debited to the accounts of the heirs of the said brothers respectively. The cost of messing is met separately by each of the four branches and likewise the expenses of marriages and education of children. No family idol being maintained by any of the separate branches of the family, no question of joint worship arises.

The Commissioner of Income-tax states that in the books of the business there is no capital account in the name of a joint family or in the name of the separate branches, but there are accounts in the names of the heirs of the said four original proprietors showing their drawings from the business. The credit side shows either nil or some paltry sum while the debit side in every case shows a large sum. The accounts of the business have never been adjusted and the accounts in the names of the heirs of the said four original proprietors have not also been adjusted. The balances are carried forward from year to year. Further the said four branches have got separate businesses of their own which are separately assessed to income-tax. In each of these assessments, a one-fourth share of the main business together with the income of the separate business of the particular branch of the family and the *bona fide* annual value of the house properties belonging to that branch are taken into account. The house properties were acquired with monies drawn from the main business debited to the account of the respective branches.

The Commissioner of Income-tax also points out that the business has throughout been assessed as an unregistered firm and that the four separate branches have filed separate returns of their own income and have been assessed separately since the year 1923-24. In July 1927, the assesseees in compliance with a notice under section 38 of the Act gave a list of "Angshidars" (the word "Angshidars" literally translated means sharers). In this return each separate branch of the family was shown to be the proprietor of one-fourth share in the business in question. It also shows not only the names of the male sharers or partners but also of female and minor partners.

On the case as submitted by the Commissioner of Income-tax it has been argued on behalf of the assesseees that in law the said four branches ought to be

* Reported as 3 I. T. C. 1.

regarded as members of a Hindu undivided family and that the business in question ought not to be assessed as an unregistered firm.

Now, every Hindu family is presumed to be joint in food, worship and estate. Under the Dayabhaga law each coparcenar takes a defined share. The essence of a coparcenary under the Mitakshara law is unity of *ownership*, whereas under the Dayabhaga law the essence of a coparcenary is unity in *possession*. So long as there is unity of possession, no coparcenar can say that a *particular* share of the property belongs to him. That he can say only after a partition. Partition then, according to the Dayabhaga law, consists in splitting up joint possession and assigning specific portions of the property to the several coparcenars. But there is no presumption that a family, because it is joint, possesses joint property or any property. Where there is joint estate and the members of the family become separate in estate, the family ceases to be joint. Mere severance in food and worship does not operate as a *séparation*. Cessar in commensality is an element which may properly be considered in determining the question whether there has been a partition, but it is not conclusive. (L.R. 31 I.A. 10; I.L.R. 31 Mad. 482). If however, after cessar in commensality any member of the family is in possession of any portion of the property separately, the presumption referred to above is considerably weakened. No doubt it is true that the mere fact that a property is purchased in the name of a member of the family and that there are receipts in his name respecting it, does not render the property by itself, his separate property; but if in addition to the fact that certain property stands in the name of one of the members, there be these further facts, namely that some other members of the family have properties standing in their separate names and are found to deal with the same as their own without reference to the rest of the family and that the members of the family are allowed to appear to the world to be the sole owners of the said separate properties, the presumption that the properties are joint is almost gone and the burden of proving that the properties are still joint will lie on those who allege that they are joint. If the family remains joint no charge can be made against any coparcenar, because in consequence of his having a larger family to maintain than others, a larger share of the joint income was spent on his family. Such expenditure is considered to be the legitimate expenditure of the whole family. If, however, the expenses of the marriages of the daughters and of the education of the children are paid for separately by the co-parceners, that is a circumstance which must be taken into consideration for the purpose of finding out whether the family still remained joint (5 B.L.R. 347).

These being the guiding considerations, each case must depend upon its own facts; and in my opinion the facts set out by the Commissioner of Income-tax taken together are only consistent with the position that the original undivided Hindu family in question has ceased to exist and that in place thereof there are four undivided Hindu families. It is not necessary to go over the facts again. But there can be hardly any doubt that specific portions of the property or specific properties have been assigned to specific coparceners. That amounts to cessation of joint estate. It is true that the monies required for the acquisition of the said properties came from the main business. But where one finds, as in this case, that the business has descended to the third generation who are in enjoyment of separate house properties and who have, in addition, separate businesses, the fact that the accounts of the main business have never been adjusted throughout these long years is not a circumstance which can be allowed to outweigh the inference properly deducible from the other facts referred to above. Further the events which have taken place since 1923-24 about the separate assessment of the said four branches can hardly be overlooked. In my opinion,

all the circumstances set out above indicate that the Income-tax authorities are right in treating the main business as an unregistered firm.

In my opinion, the assessee must lose and must pay the costs of this reference.

RANKIN, C. J.:—I agree.

BUCKLAND, J.:—I agree.

(317) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Niamat Ullah.

(8th July, 1929).

Messrs. Kajori Mal Kalyan Das

.. Assessee.*

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Indian Income-tax Act, (XI of 1922), Sec. 66—Judgment on a reference—Review application, if maintainable.

An application to review a judgment delivered on a reference to the High Court under Sec. 66 of the Income-tax Act is not maintainable.

Application [Miscellaneous Case No. 6 of 1929], to review the judgment of the High Court delivered on 5th April, 1929, reported as 3 I.T.C. 451.

K. N. Katju, and M. N. Kaul, for the Assessee.

Bajpai, for the Crown.

JUDGMENT.

This is an application by the learned Government Advocate asking us to revise our judgment delivered in an income-tax case on a statement made by the Commissioner of Income-tax under Sec. 66, Income-tax Act of 1922.

The ground on which the review is sought is this. In our judgment we found the fact stated in the "Statement of the Case", that a certain notice was issued to the assessee directing them to submit a return on a particular date. We said that this period allowed was less than 30 days, the minimum period allowed by the law. We therefore declared the assessment to be bad.

The learned Government Advocate now states that it was the practice of the Income-tax Officer concerned to state in notices issued that in the case of the period allowed proving to be less than 30 days, the assessee would have 30 days within which to make a return.

Dr. Katju on behalf of the assessee has taken a preliminary point that no review lies.

Mr. Bajpai has not been able to point out to us any rule of law by which we can entertain an application for review of judgment. He read out to us a few sentences from Lord Halsbury's Laws of England, but those sentences do not help him at all. There it is definitely said that where a judgment of the Court has been sealed, the judgment was not liable to be corrected except for

accidental slips, etc. These very provisions are contained in the Civil Procedure Code of India.

Mr. Bajpai then argued that Sec. 98, C. P. C. having been applied to the income-tax cases by Sec. 66-A of the Act, the provisions of the Civil Procedure Code are attracted. If that be so his case does not come under Sec. 114, C. P. C., for our judgment is neither a decree nor an order.

We hold that no application for review is maintainable and we dismiss the application with costs.

(318) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Niamat Ullah.

(9th July, 1929).

Messrs. Lachhman Das Babu Ram

.. Assessee.*

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Indian Income-tax Act, (XI of 1922), Secs. 22 (2) and (4), 23 (2) and (3) and 64 (1)—Enquiry under Sec. 23 (3)—Jurisdiction to issue notice under Sec. 22 (4) thereafter—Business carried on in various places—Assessment by Head-quarters Income-tax Officer—Power to call for branch returns and accounts—Report by branch Income-tax Officer, scope of—Separate notices under Sec. 22 (2) for branch income, if necessary—User of no-return form in return case, legality of—Assessment under Sec. 23 (4) on non-production of accounts—Denial of accounts by assessee.

The assessee carrying on business in Bombay, Calcutta and other places with head-quarters at Cawnpore, on an assessment by the Income-tax Officer, Cawnpore, submitted to him a return of their Cawnpore and Bombay income, while a return of their Calcutta income was submitted to the Income-tax Officer, Calcutta. In compliance with a notice under sections 23 (2) and 22 (4) issued by the Income-tax Officer, Cawnpore, on 11th August 1927 for production of the Calcutta and other branches accounts, the Cawnpore and Calcutta accounts were produced on the 26th August with an application explaining the difficulty of producing the Calcutta accounts. The Income-tax Officer after examining the accounts produced postponed the case sine die pending receipt of a report from the Income-tax Officer, Calcutta, evidently called for at the assessee's request. On receipt of this report on the 17th February, 1928, and after further examination of the Cawnpore accounts called for under section 22 (4) by notice issued on 18th February, 1928, the Income-tax Officer, Cawnpore, served a further notice on 22nd February, 1928, under section 22 (4), calling for production on 14th March, 1928 of accounts of house property income for the years S. 1981, 1982 and 1983 as well as trial balances of the Calcutta shop as on Diwali 1981, 1982 and 1983.

On the 14th March, the assessee's agent on examination by the Income-tax Officer stated that there was no account of house property income and that the trial balances could not be produced as the account books had already been produced before the Income-tax Officer, Calcutta and thereupon the case was again postponed sine die pending receipt of a further report from the Income-tax Officer, Calcutta, called for by letter dated 24th February, 1928. On the 30th

March, 1928, when the report from the Income-tax Officer, Calcutta, was received and found not to contain any trial balances or balance sheet, the Income-tax Officer, Cawnpore, called upon the assessee to produce the Calcutta accounts and on the assessee's failure an assessment was made under section 23 (4) of the Income-tax Act.

HELD, that the notices of the 11th August, 1927, and 22nd February, 1928, having been waived when the Income-tax Officer, Cawnpore, was willing to accept the report of the Income-tax Officer, Calcutta, the assessment under section 23 (4) without giving the assessee a fresh opportunity to produce those accounts was not legal.

The notice of 22nd February, 1928, under section 22 (4), was not invalid on the ground that it included accounts and documents of the Calcutta shops. Neither the form of that notice issued in Form A intended for a no-return case modified to suit the assessee's case, nor the mistake in the date mentioned therein as the date of service of notice under section 22 (2) affected its legality.

Section 22 (2) of the Act does not require that separate notices should be issued for separate places of business where an assessment is made at the headquarters of the business under section 64 (1) in respect of all the branches of the business wherever situate.

Under section 64 (1) the Income-tax Officer, Cawnpore, as the Officer responsible for the assessment of the entire business of the assessee could call for any return or accounts as he liked, although an independent enquiry had been conducted by the Income-tax Officer exercising jurisdiction at the branch office. The Income-tax Officer, Cawnpore, was not bound by the report of the Income-tax Officer, Calcutta, or to refer the matter back to the Calcutta Officer.

Where the existence of accounts called for by the Income-tax Officer was denied by the assessee it would be open to the Income-tax Officer to hold that they existed and that they had been intentionally withheld from him.

PER MUKERJI, J., (NIAMUT ULLAH, J., dissenting). An Income-tax Officer has no jurisdiction to issue a notice under section 22 (4) after the commencement of an enquiry under Sec. 23 (3).

HELD BY THE FULL BENCH, that no enquiry under Sec. 23 (3), commenced until the 14th March, 1928, when the evidence of the assessee's agent was heard on oath and hence the question referred did not arise on the facts of the case.

Case [Miscellaneous Case No. 898 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

The assessee, members of an undivided Hindu family, carry on business at various places including Bombay, Calcutta and Cawnpore; and have their headquarters at Cawnpore, which is their principal place of business, and where they are accordingly assessed to income-tax.

2. On April 22, 1926, the Income-tax Officer, Cawnpore, issued a notice under section 22 (2) of the Indian Income-tax Act (XI of 1922), requiring them to submit on or before May 31, 1927, a return of their total income in the "previous year." On May 2, 1927, he further wrote to the Income-tax Officers of all the places where the assessee were carrying on business asking them to

report the assessee's profits at those places. After applying twice for an extension of time, the assessee submitted, on August 1, 1927, a return of income in respect of their Cawnpore business only. On August 10, 1927, they submitted another return in respect of their income from their Bombay business. With regard to Calcutta business they submitted no return of income to the Income-tax Officer, Cawnpore, but submitted one to the Income-tax Officer, Calcutta; on what date is not clear from his report.

3. After receiving the returns for the Cawnpore and Bombay branches the Income-tax Officer, Cawnpore, on August 11, 1927, issued a combined notice under sections 23 (2) and 22 (4) of the Act requiring the assessee to produce, on August 15, their accounts and evidence relating to their income at Calcutta and other branch places of business. On the date fixed, Lala Brij Mohan Nath, *mukhtar-i-am* of the assessee appeared; but without the Calcutta accounts. The case was, therefore, postponed to August 26, 1927, for the production of all the accounts, including those for the Calcutta business. On August 26, 1927, accounts were produced for the Cawnpore and Bombay businesses; while with regard to the Calcutta accounts, an application was presented to the effect that it would be detrimental to the Calcutta business to send the Calcutta accounts to Cawnpore and also to send the *munib*, who was conversant with them, to explain them: since he was in sole charge of the Calcutta shop. On August 26 and 30, 1927, the Cawnpore and Bombay books were examined; and the Income-tax Officer, Cawnpore, postponed the case *sine die*, pending receipt of the report of the Income-tax Officer, Calcutta; considering that if a complete report could be secured from Calcutta, there would be no need to insist on the production of the Calcutta accounts at Cawnpore.

4. The report from Calcutta was not received until February 17, 1928. It was not accompanied by copies of the profit and loss account, or balance-sheet. The Income-tax Officer, Cawnpore, then issued another notice under section 22 (4) on February 18, 1928, requiring the assessee to produce, on February 22, 1928, along with other accounts, the accounts of the head-quarters business at Cawnpore for the year ending *Katik* 1983. The Cawnpore accounts were duly produced on this date; and their scrutiny revealed large discrepancies between the profit stated by the assessee in the return of income submitted to the Calcutta authorities and the transactions recorded in the head-quarter's account at Cawnpore. In particular, it appeared that during the *Katik* year 1982-83, on the profits of which the assessment has been made, the assessee had withdrawn no less than Rs. 34,000 from the Calcutta shop; while the profit shown in the Calcutta return of income was only Rs. 3,243-12-3. Similarly, during the *Katik* year 1981-82, the assessee had withdrawn Rs. 53,000 against Rs. 10,900—the sum assessed as the profit of the Calcutta shop. The obvious inference was that either the Calcutta shop was becoming more and more indebted, or the capital invested in that shop was being remitted to Cawnpore. The Income-tax Officer found that there was no entry of any such transference of capital in the Cawnpore accounts; and that it was impossible to ascertain the exact position from the materials before him. Accordingly, he wrote a detail letter (Appendix A*), despatched on February 24, 1928, to the Income-tax Officer, Calcutta, asking him to examine the books again, and to obtain and send to him, with his further report, copies of the trial balances of the Calcutta accounts at the close of the *Katik* years 1981-82 and 1982-83; and of the profit and loss account.

5. The Income-tax Officer also noticed that the assessee had purchased some house property in November, 1924, regarding which there was no entry in the books. He, therefore, required the assessee under section 23 (2) on Feb-

ruary 22, 1928, to explain this point. At the same time, he served a further notice on them under section 22 (4), calling for the production on March 10, 1928 of (1) accounts of income from property for the *Samavat* years 1981-82 and 1982-83; and (2) trial balances of the Calcutta shop as on *Diwali* 1981, 1982 and 1983. On March 5, 1928, one of the assessee's servants, Shambhu Nath Mehrota, who was not an authorized agent, appeared before the Income-tax Officer, Cawnpore, and stated that no accounts were maintained for the income from property. The trial balances were not produced on this date. As Shambhu Nath's statement was not legally binding on his master, the Income-tax Officer gave the assessee another opportunity to comply with the notice under section 22 (4) (issued on February 22) on March 14, 1928. On the latter date Sheo Nath, *mukhtar-i-am* of the assessee, appeared and stated (Appendix B*), that no accounts were kept for the income from property; and that the trial balances relating to the Calcutta shop, which had been asked for, could not be produced, because the account books had already been produced in Calcutta. After recording the statement of the *mukhtar-i-am*, the Income-tax Officer postponed the case *sine die*, pending receipt of a further report from the Income-tax Officer, Calcutta. This report was received on March 30, 1928, but without the trial balances and without copies of the profit and loss account, and the balance-sheet.

7. The Income-tax Officer, Cawnpore, showed this report to the assessee's representative, explained his doubts to him, and asked him to remove them by producing the accounts of the Calcutta shop, but the assessee's representative declined to do so, and asked the Income-tax Officer to refer the matter again to Calcutta. The Income-tax Officer was not prepared to take such a step on the last day but one of the official year; and since neither the Calcutta accounts, nor the trial balances, nor the accounts of the income from property had been produced, he made an assessment under section 23 (4), to the best of his judgment, on the same date, i.e., March 30, 1928. (Appendix C*).

8. Against this assessment, the assessee lodged an appeal on April 26, 1928. No appeal lies against an assessment under section 23 (4); but the assessee contended that, for various reasons which need not be set forth here, the assessment was really one under section 23 (3). The question, whether it was properly to be regarded as one made under section 23 (4), or as one made under section 23 (3) was argued at length before the Assistant Commissioner of Income-tax who came to the conclusion that the assessment had been rightly made under section 23 (4), and that, therefore, no appeal lay against it under the Act. (Appendix D*).

The assessee now desire that I should make a reference to the Honourable High Court on the following points of law (Appendix E*) (as propounded by them):—

(a) Whether the notice issued under section 22 (4) on February 22, 1928 was legally valid inasmuch as—(i) it was issued after the commencement of proceedings under section 23 (3); and that, too, for documents which were not in existence; (ii) it was issued by the Cawnpore Income-tax Officer regarding the Calcutta affair which had no relation to or bearing upon the income shown in the return here; and that, too, in form A which is *for use where a return has not been made*; (iii) no notice was served upon them on April 25, 1927, as noted in the said notice; (iv) it was not served as required by law; and (v) they were not served with any notice under section 22 (2) regarding the Calcutta income by the Income-tax Officer of Cawnpore, nor was there any return of the Calcutta income before him; and, if so, does its failure (*sic.*), if any, bring the assessment under section 23 (4)?

(b) Whether in face of the statement of Pandit Sheo Nath Pandey, petitioners' *mukhtar-i-am*, dated March 14, 1928, can it be said (*sic.*) that the notice, dated February 22, 1928, still remains uncomplied with?

(c) Whether the Income-tax authorities could, in face of the clear denial on behalf of the petitioners, presume the existence of documents mentioned in the said notice, without any evidence whatsoever on the record?

(d) Was it incumbent upon the petitioners to prepare, in compliance with the notice, the documents not in existence?

(e) Whether the Income-tax Officer of the principal place of business could compel the assessee to submit the return and also to produce the account books in connexion with the branch business before him when they are ready and willing to comply, or when they have actually complied with all the requirements of law, before the Income-tax Officer of the branch places?

(f) Whether the returns submitted by the petitioners were incomplete, and were they taken to be so by the Cawnpore Income-tax Officer; and, if so, how does it affect the present assessment?

(g) Whether the Cawnpore Income-tax Officer could impeach, or modify, or disbelieve the report of the Income-tax Officer of Calcutta; and whether, under the circumstances of the case, did he (*sic.*) legally proceed to assess the petitioner under section 23 (4)?

9. The first question, as framed by the learned counsel for the assessee, is not a mere question of law; but contains, by implication, propositions both of law and of fact that I am not prepared to admit. I cannot, therefore, state the question in the form in which it has been propounded. One allegation of fact, namely that the notice under section 22 (4) was not served as required by law, was not put forward either before the Income-tax Officer or in the grounds of appeal. Even, therefore, if it be regarded as a question of law, it cannot now be submitted for the decision of the High Court, since it does not arise out of the appellate order; and it is only in regard to points arising out of an appellate order that an assessee is entitled to claim a reference to the High Court. Another allegation, namely that trial balance-sheets for the Calcutta business did not exist, was made for the first time in appeal. It begs the question whether the Income-tax Officer and the Assistant Commissioner had sufficient grounds for presuming that they did exist; to which I shall return.

10. Question (d) does not arise since the Income-tax authorities have never contended that the assessee could be called on under section 22 (4) to create any accounts or other documents.

11. Question (f), whether the returns submitted by the assessee were incomplete, is a question of fact. The question, as a whole, is hopelessly vague. Moreover, the question that arises out of section 23 (2) is not whether the returns were incomplete, but whether the Income-tax Officer had reason to believe them to be so. The Income-tax Officer is not required by the law to state his reasons for holding that a return is incomplete, and his discretion in the matter is not subject to appeal or to control by the appellate authority. Since the question propounded is neither a question of law nor a question that can, in the nature of the case, be said to arise out of the appellate order, I am unable to state it.

12. The points of law that do arise in this case and that I now proceed to refer to the court for decision are as follows:—

- (1) Has an Income-tax Officer jurisdiction to issue a notice under section 22 (4) after the commencement of an inquiry under section 23 (3)?

- (2) Was the notice under section 22 (4) issued by the Income-tax Officer, Cawnpore, on February 22, 1928, invalid, because it included accounts and documents connected with the Calcutta shop?
- (3) Was the notice invalid (a) because it was issued in form A, intended for use where a return had not been made, though modified so as to suit the assessee's case in which a return had been made?
(b) because April 25, 1927 (the date mentioned in it) was that on which the notice under section 22 (2) was returned after service, and not that on which it was actually served on the assessee, which was apparently April 23, 1927?
- (4) Is it incumbent on the Income-tax Officer of the principal place of business, where an assessee is assessed to income-tax, to issue separate notices under section 22 (2) requiring returns in respect of the income of each branch of the assessee's business?
- (5) Was the Income-tax Officer entitled, in the face of the statement of Pandit Sheo Nath Pandey, the assessee's *mukhtar-i-am*, dated March 14, 1928, to hold that the notice under section 22 (4), dated February 22, 1928, had not been complied with?
- (6) When an assessee denies the existence of accounts or documents, may the Income-tax Officer presume the existence of such accounts or documents?
- (7) Has the Income-tax Officer of an assessee's principal place of business jurisdiction to compel such assessee to submit a return and produce accounts in respect of a branch business when he has submitted a return, produced accounts, and otherwise complied with all the requirements of the law before the Income-tax Officer of the place where he has such branch business?
- (8) Is the Income-tax Officer of the principal place of business bound to accept the report of the Income-tax Officer of a place where an assessee is carrying on a branch business? If not, is he bound to refer the matter back to the latter officer for further enquiry and not to assess according to his judgment?
- (9) In all the circumstances of this case, was the assessment rightly made under section 23 (4)?

13. On the first point I am of opinion that there is clearly no restriction in the Act as to the stage at which a notice under section 22 (4) may be issued, except that it can only be issued (except where the assessee is the principal officer of a company) after a notice has been served under section 22 (2). This view has recently been held by your Lordships in the case of *Lala Chandra Sen Jaini* (1) and by the High Courts of Calcutta and Patna in the cases of *Harmukhrai Duli Chand* (2) and *Ram Khelawan Ugam Lal* (3). I invite your Lordship's attention to those decisions.

14. *Point 2.*—It was held by this Honourable Court on a previous reference, arising out of the assessment of these very assessee, that the Income-tax Officer, Cawnpore, where the assessee was assessed, had jurisdiction to call for a return of the income of the Calcutta business; and of, or the accounts relating to it. The notice under section 22 (4), issued by the Income-tax Officer, Cawnpore, was

(1) 8 I. T. C. 11.
(2) 3 I. T. C. 198.
(3) 3 I. T. C. 225.

not, therefore, invalid because it referred to Calcutta accounts or documents (vide *Lachman Dass Babu Ram v. The Commissioner of Income-tax, U. P.* (1).

15. *Point 3.*—Form A is not a statutory form but one prescribed by the Central Board of Revenue in the exercise of its general functions of administration. The Act does not require that any form should be prescribed for the notice. The notice under section 22 (4) would, therefore, have been equally valid if it had been issued on plain paper. The objections taken to the notice are, therefore, frivolous. The error, if any, regarding the date on which the notice under section 22 (2) was served, is absolutely immaterial.

16. *Point 4.*—A notice under section 22 (2) requires the assessee to make a return in the form prescribed by statutory rules of his total income. "Total income" is defined in section 2 (15) as the "total amount of income, profits and gains from all sources to which this Act [Income-tax Act (XI of 1922)] applies" The suggestion, that separate returns should be called for for separate places of business, is absolutely devoid of any foundation in the statute; and is, in fact, entirely contrary to its general scheme.

17. *Point 5.*—The statement of Pandit Sheo Nath Pandey was evasive and indefinite; and it is, I submit, perfectly obvious that it cannot be regarded as legally conclusive. The Income-tax Officer and the Assistant Commissioner had before them the assessment order for 1924-25, in which year regular accounts for income from property were produced before the Income-tax Officer, Cawnpore. The income from property is derived from a number of houses, and admittedly amounts to as much as Rs. 6,000 net, after making all statutory deductions; and it seems improbable that so extensive a property could be managed without accounts. The Pandit was evidently not a person with special knowledge of matters relating to the house property; for he admitted that he did not even know which houses assesseees owned. The Income-tax Officer and the Assistant Commissioner had, therefore, I submit, adequate grounds for disbelieving the Pandit's statement that there were no accounts for property especially since the assesseees themselves did not volunteer any statement on the subject. As for the trial balances, even the Pandit was not prepared to commit himself to a definite denial of their existence. I, therefore, submit that the Income-tax Officer and the Assistant Commissioner were fully justified in drawing the inferences that they have drawn in regard to these two questions of fact.

18. *Point 7.*—This is covered by what I have said on point 2 in paragraph 14 above, and by the ruling of this High Court there quoted. The Calcutta accounts were necessary to explain the circumstances mentioned in paragraph 4 above.

19. *Point 8.*—It is on the Income-tax Officer of the principal place of business that the statutory duty of making a correct assessment is laid; and there is no foundation whatever in the Act for the suggestion that he is bound by the reports of officers at other places of business who have, to a limited extent, concurrent jurisdiction.

20. *Point 9.*—The assesseees clearly failed to comply with the notice under section 22 (4), issued on August 11, 1927, calling for the production of their Calcutta accounts. This default justifies the assessment under section 23 (4).

21. I am, therefore, of opinion that points nos. 1, 5, 6, 7 and 9 should be answered in the affirmative; and points Nos. 2, 3, 4 and 8 in the negative.

Dr. Katiya, for the Assesseees.

Bajpai, for the Crown.

JUDGMENT

MUKERJI, J.:—This is a reference by the Commissioner of Income-tax, United Provinces, under section 66 (2) of the Income-tax Act of 1922.

The case sent up for expression of opinion on the part of the High Court is fully stated in the "statement of the case" submitted to us and very briefly is as follows:—The assessees, at whose instance the reference has been made, carry on business at Cawnpore, Bombay and Calcutta with head-quarters at Cawnpore. Under Sec. 64 sub-section (1) of the Income-tax Act, the Income-tax Officer of Cawnpore had the right and power of assessing the income-tax, because Cawnpore was within his jurisdiction. The Income-tax Officer of Cawnpore, on April 22nd, 1927, issued a notice under Sec. 22 (2) of the Indian Income-tax Act requiring the assessees to submit a return of their total income in the "previous year". The previous year in this case was from Dewali of 1925 to Dewali of 1926 as the account year of the assessees commenced on the 1st day after the Dewali festival of a Hindu year. On different occasions the assessees submitted returns for Cawnpore and Bombay. With regard to Calcutta business they submitted no return to the Officer at Cawnpore but submitted one to the Officer in Calcutta. On 11th August 1927, the Income-tax Officer of Cawnpore issued a combined notice under Secs. 23 (2) & 22 (4) of the Act requiring the assessees to produce on 15th August their accounts and evidence relating to their income at Calcutta and other branch places of business. On 26th August 1927, accounts were produced for Cawnpore and Bombay business while with regard to the Calcutta accounts, an application was presented to the effect that it would be detrimental to the Calcutta business to send the Calcutta accounts to Cawnpore and also to send the munib who was conversant with them to explain the account. It was stated that the munib was in the sole charge of the Calcutta business. After examining the Cawnpore and Bombay books the Income-tax Officer of Cawnpore postponed the case *sine die* pending receipt of a report of the Income-tax Officer of Calcutta, which report, he had evidently called for at assessees' request. He thought that if a complete report was received from Calcutta, "there will be no need to insist on the production of the Calcutta accounts at Cawnpore". The report from Calcutta was received on 17th February 1928. The Income-tax Officer in Cawnpore thought that it was not complete and it was not accompanied with certain documents which he thought were necessary for him to see in order to arrive at a proper estimate of the assessees' income. These were copies of profit and loss account. Thereupon the Cawnpore Officer issued another notice under Sec. 22 (4) on 18th February 1928, requiring the assessees to produce on 22nd February 1928 the accounts of the head-quarters business at Cawnpore. The Cawnpore accounts made him suspicious of the correctness of the report received from Calcutta. He also thought that he should have a statement of the account of house property at Cawnpore. He accordingly served a further notice again under Sec. 22 (4) calling for the production on 10th March 1928 of accounts of income from property (house property) for the sambat year 1981 to 1982 and 1982 to 1983 and two trial balances of the Calcutta shop as on Dewali 1981, 1982 and 1983. On 14th March 1928 the assessees' Mukhtar-i-am (general agent) Sheonath appeared and stated that no account of income from house property at Cawnpore was kept and that the trial balances relating to Calcutta shop could not be produced because the account books had already been produced before the Income-tax Officer at Calcutta. On this statement the case was again postponed *sine die* pending receipt of a further report from the Income-tax Officer of Calcutta. On 30th March 1928 a report was received from the Income-tax Officer of Calcutta but there was no "trial balances" or profit and loss account or the balance sheet. On the same date, the Income-tax Officer of Cawnpore asked the representative of the assessees to explain his doubts and to produce the

accounts of the Calcutta shop. The representative declined to do so and asked the Income-tax Officer to refer the matter again to Calcutta. This the Cawnpore Officer declined to do and, as the financial year was closing, he assessed a tax "to the best of his judgment" on the same date, i.e., 30th March 1928. The Cawnpore Officer purported to act under Sec. 23 (4) of the Act.

The assessee went up in appeal to the Assistant Commissioner of Income-tax. That Officer held that no appeal lay to him as the assessment had been rightly made under Sec. 23 (4) of the Act. Thereupon the assessee asked the Commissioner to make this reference and the Commissioner accordingly sent up the following questions for the opinion of the High Court. These are:—

- (1) Has an Income-tax Officer jurisdiction to issue a notice under Sec. 22 (4) after the commencement of an inquiry under Sec. 23 (3)?
- (2) Has the notice under Sec. 22 (4) issued by the Income-tax Officer, Cawnpore, on February 22nd 1928, invalid, because it included accounts and documents connected with the Calcutta shop?
- (3) Was the notice invalid (a) because it was issued in form A, intended for use where a return had not been made, though modified so as to suit the assessee's case in which a return had been made? (b) because April 25, 1927 (the date mentioned in it) was that on which the notice under Sec. 22 (2) was returned after service, and not that on which it was actually served on the assessee, which was apparently April 23, 1927?
- (4) Is it incumbent on the Income-tax Officer of the principal place of business where an assessee is assessed to income-tax, to issue separate notices under section 22(2) requiring returns in respect of the income of each branch of the assessee's business?
- (5) Was the Income-tax Officer entitled in the face of the statement of Pandit Sheo Nath Pandey, the assessee's *Mukhtar-i-am*, dated March 14, 1928 to hold that the notice under Sec. 22 (4) dated February 22, 1928, had not been complied with?
- (6) When an assessee denies the existence of accounts or documents, may the Income-tax Officer presume the existence of such accounts or documents?
- (7) Has the Income-tax Officer of an assessee's principal place of business jurisdiction to compel such assessee to submit a return and produce accounts in respect of a branch business when he has submitted a return, produced accounts, and otherwise complied with all the requirements of the law before the Income-tax Officer of the place where he has such branch business?
- (8) Is the Income-tax Officer of the principal place of business bound to accept the report of the Income-tax Officer of a place where an assessee is carrying on a branch business? If not, is he bound to refer the matter back to the latter officer for further enquiry and not to assess according to his judgment?
- (9) In all the circumstances of this case, was the assessment rightly made under section 23 (4)?

Before I proceed to answer the several questions, it will be necessary to find out the meaning and application of Secs. 22 (4) and 23 (4) of the Income-tax Act, for practically the whole controversy ranges over those two sections. I will

refer to decisions of this Court and other courts later on, for I want, for the present, to examine, for myself the language of the law independently of and untrammelled by any opinion of other judges.

The controversy relates to the import of Sec. 23 (4). The question is in what cases an appeal is allowed and in what cases an appeal is not allowed? The assessee's sole grievance is that they had the right to lay their case before the Asst. Commissioner and they have been unjustly shut out from the exercise of such a right. The Income-tax Officer of Cawnpore purported to act in making the assessment, under section 23 (4) "to the best of his judgment". Under section 30 of this Act no appeal lies where an Income-tax Officer is entitled to make and does make an assessment to the best of his judgment.

Sec. 23 (4) runs as follows: "Ifanyperson fails to make a return undersub-section 2 of section 22or fails to comply with all the terms of a notice issued under sub-section 4 of the same section, or *having made a return*, fails to comply with all the terms of a notice issued under sub-section 2 of this section, the Income-tax Officer shall make the assessment to the best of his judgment." A plain reading of sub-section 4, section 23 would suggest that there are three cases in which an Income-tax Officer is entitled to "make assessment to the best of his judgment". They are (I am not mentioning the case of a company) :—(1) when a proposed assessee fails to make a return under section 22 (2), (2) where he fails to comply with all the terms of a notice issued under sub-section 4 of section 22, and (3) fails to comply with all the terms of a notice issued under sub-section 2 of section 23. These three occasions, it will be noticed, are enumerated in the same order in which the rules for asking for a return or compliance with a notice are enacted. The rule as to calling for a return comes first and is the first of the occasions mentioned in section 23 (4). The issue of a notice under section 22 (4) comes after the provision as to calling for a return and is the second occasion mentioned in section 23 (4). The provision for issue of notice under section 23 (2) comes last and is the third occasion mentioned in section 23 (4). Ordinarily, it would be expected that the three occasions would come in order of time, the notice for return first, then the notice for accounts and documents and then the notice for production of evidence. If there were any doubt in the matter, these doubts are completely removed by the use of the four words, "having made a return", to be found in section 23 (4). Those words, if they have any meaning at all, indicate that the first two occasions for making an assessment to the best of the Income-tax Officer's judgment come before the third occasion may possibly appear.

The learned Government Advocate has argued that the words "having made a return" in section 23 (4) have really no significance and to quote the language of one of the cases cited before us, they are 'harmless'. In my opinion this is a method of construction which must not be allowed to prevail.

It is an established rule of construction of statutes that where the meaning is plain, it is not open to any party to read the rule of law in any way other than what is dictated by the plain meaning of the enactment. See page 66 of Craies' Statute Law (1923). I shall have occasion to refer to this book more than once. It cannot be doubted that the words "having made a return" if allowed to remain where they are, suggest that the first two occasions for making an assessment to the best of judgment come before the third occasion for the purpose comes. If that be so, it will not do to say that those four words have been used unnecessarily as a mere tautology or as "harmless" words. Craies at page 98 quotes the following from Lord Brougham: "A statute is never supposed to use words without a meaning". Then he quotes from Erle C. J. "To reject words as insensible is the *ultima ratio* when an absurdity would follow from giving effect to the words of an enactment as they stand" (*ibid*). Again, Lord Holt is quoted

as having said: "I think we should be very bold men when we are entrusted with the interpretation of Acts of Parliament, to reject any words that are sensible in an Act". It will be seen from the above quotations which are from very high authorities, that unless and until the language used in a statute makes the meaning entirely insensible, every word used must be given its plain meaning.

It has however been urged that the plain meaning of the words "having made a return" cannot be given effect to for this reason. Sec. 22 (4) is worded in language without limit of time and, therefore, it would not do to import into it a limit of time. In other words, it is urged that a notice under Sec. 22 (4) of the Act may be issued at any time, even after an enquiry under Sec. 23 of the Act has started. I agree that if Sec 22 (4) stood by itself, it would be uncontrolled by any time limit. But is not a time limit imposed by the four words, "having made a return" already quoted?

If there be any obscurity in an enactment, an apparent contradiction, the meaning of the Act has to be found within the four corners of the Act itself. Caries quotes from Coke the following (see p. 92): "The office of a good expositor of an Act of Parliament is to make construction on all the parts together and not of one part only by itself....." and again, at p. 93: "It is the most natural and genuine exposition of a statute to construe one part of a statute by another part of the same statute, for that best expresseth the meaning of the makers...." Again, at p. 93 the learned author quotes the following from a case decided by Sir John Nicholl: "The key to the opening of every law is the reason and spirit of the law; it is the *animus imponentis*, the intention of the lawmaker expressed in the law itself, taken as a whole." Supposing then that the rule in Sec. 22 (4) is unlimited by time, and Sec. 23 (4) does impose a limit of time, let us assume there is a little obscurity. What are we to do? Are we to reject the express words of Sec. 23 (4) in order to hold that Sec. 22 (4) is uncontrolled by time limit? That would be sacrificing one part in order to read another part of the same enactment in a particular way. Would it not be a better method of reading the Act to make the whole consistent and to say that although there is no time limit in Sec. 22 (4), a time limit is brought in by Sec. 23 (4)

Now let us see if there is any sense in putting a time-limit on Sec. 22 (4), as in my opinion, Sec. 23 (4) does. What is the effect, after all, of Sec. 22 (4) being not complied with? It is that the assessee is shut off his right to appeal. There is no other consequence. Is the right to appeal taken away, as a matter of punishment or from some other motive? In an unreported Madras case,* read out to us by the learned Government Advocate as a part of his argument a learned judge thought that it was by way of a penalty for non-compliance of the Income-tax Officer's order, that the appeal is shut out. With all respect, I find nothing in the Income-tax Act which says that the appeal is to be shut out as a matter of punishment. Unless an Income-tax Officer is actuated by malice or chagrin on account of the non-compliance with his order, he will, if he does his duty, assess a tax, which, in his opinion, would be just and fair. "To the best of his judgment" does not imply any penal imposition of tax but what is only a fair and reasonable tax, having regard to all the information as to circumstances the Income-tax Officer may possess without any formal enquiry. It must, therefore, be taken that the rule shutting out an appeal was not meant for the punishment of the assessee. By way of analogy, I may point out that under the Civil Procedure Code, no appeal is allowed where a decree followed a compro-

* Since reported as *Ramaswami Chelliar v. Commissioner of Income-tax, Madras* 81 T. C. 220.

mise or a decree followed an award. Surely, the parties do not commit any contempt of court by coming to terms, nor do they commit any contempt of court by entering into a reference to arbitration which is followed by an award. Similarly, there is no appeal from the verdict of the jury in a criminal case except as to punishment, with which the jury have nothing to do. The principle underlying the shutting out of an appeal in all such cases is the same, namely there is nothing which can be taken before a court of appeal for the exercise of its judgment. Where the parties come to terms, no benefit can be reaped by an appeal. Where an award is made, the judgment is given by the chosen arbitrator of the parties and the court of appeal cannot be called upon to exercise its own judgment. An arbitrator in coming to his decision is not fettered by rules of evidence. The result is, the appeal is shut out because there is no fit case, there are no proper materials on which the appellate court may exercise its judgment. Similarly, in a jury trial, the jury do not give any reasons for their verdict. Nobody knows how they are influenced and how they discussed the matter among themselves. There is no room for any appellate court to exercise its jurisdiction.

Coming back, then, to the case before us, we find that the appeal has been shut out only where there are no materials which can be properly placed before an appellate Income-tax Officer. To start with, where the proposed assessee makes no return of his income, there is no right of appeal. The reason is plain. What are the materials to be placed before the appellate officer to exercise his judgment on? The information on which the Income-tax Officer has assessed the proposed assessee is, so to say, "extra-judicial" and cannot be disclosed and cannot be made the subject matter of scrutiny by the appellate officer. Again, if the proposed assessee has not furnished the Income-tax Officer with the accounts and documents as required by the officer under Sec. 22 (4) of the Act, there is no material besides any private information that the Income-tax Officer may possess for assessing the tax. Before the Income-tax Officer can examine, with any chance of accuracy, a return submitted by an assessee with whose antecedents he is not acquainted favourably, he might require the proposed assessee to submit his accounts and documents. Where an Income-tax Officer knows his assessee sufficiently well and has a favourable opinion about him, he would be content with simply asking for a return. Where the Income-tax Officer has not got a favourable opinion of his proposed assessee or has no definite opinion either way, i.e., either in his favour or against him, he might think it desirable to have the assessee's accounts and documents before him, in order to decide whether he would accept the return or would hold an enquiry as to its correctness. If the assessee fails to submit the accounts and the documents required he does not put the Income-tax Officer in a position to form a definite judgment and the only thing that remains open to the officer is to act "to the best of his judgment", which means in plain words, to act on such information obtained privately as he may possess. In such a case, to allow an appeal would be meaningless. The appellate officer would have no materials on which to go. Again, where the Income-tax Officer is not satisfied with the return submitted by the assessee, possibly even after its scrutiny with the aid of the assessee's accounts and documents, he would decide to hold an enquiry. Where he wants to hold an enquiry and the assessee does not help him with materials and evidence, here again there is nothing for the taxing officer to go upon except his own judgment which again means unverified and unsubstantiated information. Here, again there will be no sense in allowing an appeal; for the appellate officer would have no materials on which to form judgment. Apparently, the accounts and documents called for under section 22 (4) would not be sufficient to satisfy the doubts of the taxing officer, for it must be taken that they have been examined and have been disbelieved. By themselves, then, those documents would not furnish any

proper criteria for investigation. But where an enquiry has started and has been conducted at least partially, there would be materials on the record which might fairly be submitted to the consideration of an appellate officer. It is in the last mentioned case alone that an appeal would be allowed with justification.

It is hardly conceivable that it was considered to be just that an appeal should be shut out in a case like the following. Suppose an enquiry has gone on, in the case of a large business, for ten days. On the eleventh day, the Income-tax Officer wants a particular book of the proposed assessee. For some reason, good, bad or indifferent, the assessee fails to produce that book. If, at that stage, the Income-tax Officer says that he would make an assessment "to the best of his judgment", he would not be making the assessment on such information alone as he possessed before the enquiry began, but on information which was placed before him. The assessee may then fairly say that having supplied materials, he should be allowed to go before an officer of greater experience, for his judgment by way of appeal. As I have said, it is inconceivable that the legislature should have meant that a prolonged enquiry should come to nothing and should not be subjected to appellate judgment simply because the assessee, at one moment, failed to produce a certain document. On principle therefore, and on reading, as a whole, the two sections 22 & 23, it seems to be abundantly clear to me that a right to make an assessment to the best of the officer's judgment cannot be made after an enquiry has been started, so as to shut out an appeal, simply because at any time after the enquiry has been started the assessee fails to produce a certain document or account.

It has been urged that section 22 (4) is a very useful provision and it should be open to the Income-tax Officer to use it at all times even in the case of investigation indicated by sub-sections 2 & 3 of section 23. There can be no doubt that an Income-tax Officer should have the power to call for documents and all information that he may require for a proper and just assessment. For this purpose he has been invested with the powers of a civil court by section 37 of the Income-tax Act itself. If he has all the powers of a civil court trying a suit, why can he not ask the assessee under those powers, to produce the very accounts and documents which he thinks are needed for a fair assessment? Surely, a civil court can call upon a party to produce any document in his possession or power. The power of the Income-tax Officer to call for documents and accounts is not limited by the language of section 23 (3) of the Income-tax Act, or even by sub-section 4 of section 22. If section 22 (4) was meant to be only a part of the power of an officer in holding an inquiry, its proper place would have been in section 37. The whole question is, in what cases an appeal has been allowed by the Act and in what cases they have not been allowed?

I need not repeat what I have already stated, namely, an appeal has been shut out only when it would serve no useful purpose. That is to say, an appeal has been shut out where the appellate officer would have no material on which to decide a case. But where materials are on the record, whether sufficient or insufficient, an appeal has been allowed.

I may mention here that one of the main reasons which has actuated the learned judge of different High Courts to hold that section 22 (4) must be unlimited in its application in point of time, is that it is a useful rule of law, which must be made use of by the Income-tax Officer for the benefit of the assessee himself. Those learned judges, with all respect to them, have overlooked—at least have not quoted in their judgment—the provisions of section 37 of the Income-tax Act which confers on the Income-tax Officer all the powers of a civil court trying a suit. Certainly it may happen that an order made in the course of the enquiry by the Income-tax Officer for the production of a docu-

ment is disobeyed. Even in such a case, the Income-tax Officer will be entitled to draw such adverse inference, as he may, from the disobedience; but nonetheless, his decision will be a decision on the merits of the case, on such materials as are before him, and, in such a case, an appeal will be permitted under the Act. It will be noticed that even under the Civil Procedure Code, where a party is in contempt by non-production of documentary evidence in his possession or power or by not giving evidence, the court is empowered to pronounce judgment against him, but such judgment is open to appeal (See Order 16 R. 20 and Order 43 R.1 (h) of the Civil Procedure Code). It must not be forgotten that there are two distinct classes of cases. In one class there is no enquiry at all owing to the proposed assessee's default. In such a case there will be no sense in granting an appeal and there is no appeal. In the other class, there is some material before the assessing officer, *plus* some want of material owing to the assessee's default. In the latter case, an appeal would be granted, because after all, there is something on which the appellate officer may form his own judgment and may be disposed to modify the judgment of the Income-tax Officer.

Another principle bearing on the interpretation of statutes must not be overlooked in interpreting the Indian Income-tax Act, which is a purely fiscal enactment. It is the ordinary privilege of a subject that he shall not be taxed on his income without a proper investigation. It is but an elementary right of the subject that it should be open to him to prove what his income is, before he is assessed on the income. If it had been the intention of the legislature that the mere word of the taxing officer should be final, one should find a clear indication of that in the language of the statute. Craies in his invaluable book on interpretation of Statute Law says at p. 105 "Express and unambiguous language appears to be absolutely indispensable in statutes passed for the following purposes:—(1) imposition of tax.....(3) Altering or excepting from the operation of clearly established principles of law....." If the meaning of Sec 22 (4) read with Sec. 23 (4) is this that the power of an Income-tax Officer should be allowed to hang, like the sword of Democles, on the head of the proposed assessee, to be applied at any time to shut out an enquiry by the appellate court and for the acceptance, as final word, of the Income-tax Officer's assessment, we should expect the clearest language being employed for the purpose. As against the argument that the sub-section 4 of section 22 is a very useful rule and should not be limited in its operation by the four words "having made a return" to be found in sub-rule 4 of section 23, the following may be usefully quoted from Craies' book at p. 106:—".....if there be admissible, in any statute, what is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute". As I have already said, there is no necessity to press Sec. 22 (4) into the service of the Income-tax Officer holding an enquiry under Sec. 23. He has ample powers for the purpose of the enquiry, the same powers which a civil court has got in trying a suit.

As for authority on the interpretation of Secs. 22 (4) and 23 (4) the majority of them are in favour of reading Sec. 23 (4) as if the words "having made a return" did not exist in the section. The case of *Kushi Ram v. The Commissioner of Income-tax* (1) takes the same view as I have taken. All other cases, including a two judges case of this Court, viz., *Chandra Sen Jaini v. The Commissioner of Income-tax U. P.* (2) practically take the view that the words "having made a return" have no force of their own, they are "harmless" or mere surplusage. These cases are *Harmukhrai Dulichand v. The Commissioner Income-tax, Bengal* (3) and *Ram Khelawan Ugam Lal v. The Commissioner of*

(1) 2 I.T.C. 517.

(2) 3 I T. C. 17.

(3) 3 I. T. C. 198.

Income-tax, Bihar & Orissa(1). It would serve no useful purpose to take the arguments of the learned judges one by one in the several cases and to attempt to dissect them. If, however, these cases are examined, it will be found that the words "having made a return" are a mere surplusage, or that Sec. 22 (4) is a useful piece of rule and the Income-tax Officer should not be deprived of its use. It has indeed been pointed out that the use of the rule is for the benefit of the proposed assessee himself. I have already pointed out that we have no right to throw away the language of a statute, especially of a fiscal statute, as a mere surplusage. I have pointed out that a clear and consistent meaning can be given to both Secs. 22 (4) & 23 (4) of the Act. I have pointed that the Income-tax Officer has got ample power in the course of an investigation held by him under section 23 to call for any document or evidence or accounts from the assessee. Such being the case, with utmost respect, I am unable to agree with the view taken in this Court, or in the courts in Patna, Madras and Calcutta. If the points that have struck me, as very very material and as fully answering the objections and arguments of the learned judges had been considered by them, I would certainly have bowed to their decisions. But as things stand, the arguments that weigh with me have not been considered, at least in their entirety, by the learned judges and my inability to accept the view of so many eminent judges, I trust, is fully justified.

I would now come to the several questions put by the Commissioner of Income-tax and attempt to answer them. In view of a general discussion of the law given above, I will not discuss the reasons of the answers except where they are really necessary.

Question No. 1: My answer is an emphatic no.

Question No. 2: My answer is that the notice is invalid not because it included accounts and documents connected with the Calcutta shop, but because the issue of such a notice was illegal after an enquiry had commenced under section 23 (3).

Question 3 (a): My answer is that the form used is immaterial. The invalidity lies in the issue of the notice after the enquiry had started.

Question 3 (b): Answer:—The date was not material and does not affect the issue of the notice, if it was otherwise valid.

Question No. 4: Answer:—Section 64 (1) of the Income-tax Act authorises the Income-tax Officer at Cawnpore to assess the income-tax at head-quarters for all the branches of the business wheresoever situated and there is nothing in section 22 (2) which requires that separate notices should be issued for separate places of business.

Question No. 5: Answer:—It was open to the Income-tax Officer to disbelieve Sheonath Panday when he stated that no account book was kept and to hold that one was kept. It was also open to the Income-tax Officer to hold, as to the account sheets of Calcutta, that his order had not been complied with. This answer, however, is subject to the answer given to question No. 1, viz., the notice was illegal.

Question No. 6: Answer:—It must depend entirely on the circumstances of the case. No general answer can be given which can be applied to every case. In this particular case, I have replied to question No. 5 that the Income-tax Officer would be justified in holding that there was an account book showing the income from the house property at Cawnpore and that it has been intentionally withheld from him.

Question No. 7: My answer to this question is that having regard to the language of section 64 (1) of the Income-tax Act, the only officer who is responsible for a correct assessment for the entire business of the assessee is the Cawnpore Officer and for the purpose of assessment he can call for any returns and accounts he likes, although an independent enquiry has been conducted by the Income-tax Officer exercising jurisdiction at the locations of the branch offices of the assesseees. This was the opinion given by this Court in *Lachman Prasad v. The Commissioner of Income-tax, U.P.* (1). I would add that the rider which was added in the case just quoted, viz., the powers of the authorities at the head-quarters should never be exercised oppressively, so that persons willing to submit to an enquiry at the branch office should not, ordinarily, be compelled to bring their documents and officers all the way to the head office from distant places like Calcutta and Bombay. The Act should be administered as inoppressively as may be possible, always having an eye to the convenience of the subject whom it is proposed to tax.

Question No. 8: As already stated in answer to question No. 7, although the Officer at Cawnpore was not an appellate officer to the Officer in Calcutta, yet the Cawnpore Officer was not bound by the report of the Calcutta Officer and was not bound to refer the matter back to the Calcutta Officer. As regard the assessment according to one's judgment the assessment should always be on the merits after an enquiry has started and not "according to judgment" (if that is meant to shut out an appeal).

*Question No. 9: Answer:—*No. The Income-tax Officer was bound to pronounce judgment, on the merits, so as to allow of an appeal.

NIAMAT ULLAH, J.:—This is a reference under section 66 (2) of the Income-tax Act 1922, made by the Commissioner of Income-tax for decision of certain questions of law arising under the following circumstances:—

Messrs. Lachhman Das Babu Ram, the assesseees, carry on business at three places, viz., Cawnpore, Bombay and Calcutta, the first named being the principal place of business where they have been assessed to the income-tax to which the reference relates. They were required by a notice issued on 22nd April 1927 under section 22 (2) of the Income-tax Act to submit on or before the 31st May 1927 a return of their total income in the previous year. On the 2nd May 1927, the Income-tax Officer who had issued the notice already mentioned wrote to the Income-tax Officers of Bombay and Calcutta asking for reports in regard to the assesseees' profits at those places. On the 1st August 1927, the assesseees submitted a return in respect of their income derived from the Cawnpore concerns. Subsequently they submitted a similar return with regard to their income of the Bombay business. They did not make any return to the Income-tax Officer, Cawnpore, regarding their profits derived from the Calcutta branch, but did so to the Income-tax Officer, Calcutta. On the 11th August 1927, a combined notice under sections 22 (4) and 23 (2) was issued requiring them to produce their accounts relating to the Calcutta branch and such evidence as they desired to adduce in support of their return. On the 26th August 1927, accounts relating to their business at Cawnpore and Bombay were produced but not those relating to the Calcutta branch. On the 17th February 1928, a report was received from the Income-tax Officer of Calcutta in respect of the assesseees' income derived from the Calcutta business. This did not satisfy the Income-tax Officer of Cawnpore who obtained the production of the assesseees' accounts maintained for the head-quarters of their business, viz., Cawnpore. This led to certain discoveries and a notice under section 23 (2) was issued on 22nd February 1928, calling upon the assesseees to produce accounts relating to "property"

and trial balances of receipts and disbursements in respect of the Calcutta concern for a certain period. On 5th March 1928, it was stated on behalf of the assessee that no account was kept of the income of such property. The trial balances requisitioned were also not furnished. On the 14th March 1928, certain proceedings were taken by the Income-tax Officer, Cawnpore, to whom Sheo Nath, the general agent of the assessee, definitely stated that no account was kept for the income of "property" and that the trial balances relating to the Calcutta shop could not be furnished as the accounts relating to that shop had already been produced before the Income-tax Officer, Calcutta. After some correspondence between the Income-tax Officer, Cawnpore, and that of Calcutta an assessment was made on the 30th March 1928. The income of the Calcutta branch was assessed at Rs. 40,000 under section 23 (4). The significance of assessment under section 23 (4) is that it is based on the "best judgment" of the Income-tax Officer and that no appeal lies from such an assessment. An appeal, was, however, preferred from this assessment on the ground that it could not in law be considered to be one under section 23 (4) so as to deprive the assessee of the right of appeal. The Assistant Commissioner who heard the appeal in the first instance, ruled that section 22 (4) applied and that the appeal was incompetent. A further appeal to the Commissioner led to the reference under consideration.

The questions which emerge from this statement of facts and which we are called upon to decide are nine in number and are mentioned at pages 5 and 6 of the statement of facts submitted by the Commissioner with his own opinion. The answers to these questions largely depend on a consideration of sections 22 (2) and (4) and 23 which are quoted below:—22 (2) In the case of any person other than a company whose total income is, in the Income-tax Officer's opinion, of such an amount as to render such person liable to income-tax, the Income-tax Officer shall serve a notice upon him requiring him to furnish, within such period, not being less than thirty days, as may be specified in the notice, a return in the prescribed form and verified in the prescribed manner setting forth (along with such other particulars as may be provided for in the notice) his total income during the previous year.

(4) The Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2), a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require:—Provided that the Income-tax Officer shall not require the production of any accounts relating to a period more than three years prior to the previous years.

23. (1) If the Income-tax Officer is satisfied that a return made under section 22 is correct, and complete, he shall assess the total income of the assessee, and shall determine the sum payable by him on the basis of such return.

(2) If the Income-tax Officer has reason to believe that a return made under section 22 is incorrect or incomplete, he shall serve on the person who made the return a notice requiring him, on a date to be therein specified, either to attend the Income-tax Officer's office or to produce, or to be caused to be there produced any evidence on which such person may rely in support of the return.

(3) On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, the Income-tax Officer, after hearing such evidence as such person may produce and such other evidence as the Income-tax Officer may require, on specified points, shall, by an order in writing, assess the total income of the assessee, and determine the sum payable by him on the basis of such assessment.

(4) If the principal officer of any Company or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, as the case may be, or fails to comply with all the terms of a notice issued, under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment.

The first question which calls for a decision of this Court has been stated in these terms:—"Has an Income-tax Officer jurisdiction to issue a notice under section 22 (4) after the commencement of an enquiry under section 23 (3)?" The contention before us has gone further and it has been argued that notice under section 22 (4) cannot be issued after a return required by section 22 (2) has been made. In this view section 22 (4) applies only to cases where for some reason not easily conceivable, the Income-tax Officer desires inspection of the assessee's account before he has any idea of the sources of their income, of the amount of their income and of the contingency of the accounts being needed to test the correctness of the figures to be mentioned in the return. Section 22 (4) clearly lays down that a notice under that section can be issued to "any person upon whom a notice has been served under sub-section (2)", i.e., to any person who has been previously called upon to furnish a return. The scope of the section is thus narrowed down to the absurd limits of the time after a notice for return has been served and before the return is made. It will be observed that notice under section 22 (4) can be issued only to a person who has been previously required to furnish a return, and if the contention put forward on behalf of the assessee is sound, notice under section 22 (4) cannot be issued after a return has been made. I am unable to accept such a reading of section 22 (4), otherwise quite general and unqualified as regards time, which leads to the result I have indicated and which can hardly serve any useful purpose in making an assessment. To give effect to the interpretation contended for on behalf of the assessee we have to insert some such words as "and who has not made the return" after the words "sub-section (2)". It is one of the elementary rules of construction of statutes that it should be so read as to avoid introducing what the Legislature has not thought fit to introduce, and that a construction which has that effect should be rejected. Section 23 (1) which follows it makes it quite clear what the object of a notice under section 22 (4) is. On receipt of a return the Income-tax Officer may either accept it forthwith or may, if so advised, verify its correctness with reference to the accounts for which a requisition may be made under section 22 (4) at that or any other stage.

There is likewise no reason to confine the scope of section 23 (4) to the period before the commencement of an enquiry initiated by section 23 (2). It is conceded that the section itself does not warrant such a restriction. It is true on the other hand that ordinarily the requisition contemplated by section 22 (4) will be made on receipt of the return so as to avoid an enquiry if possible. In majority of cases the Income-tax Officer will call for accounts on receipt of a return which is *prima facie* unsatisfactory and before an enquiry is decided on. But cases may occur in which after the commencement of such enquiry the necessity of examining the accounts may be felt. Cases are also conceivable where accounts are not expected to remove doubts altogether and yet they cannot be dispensed with. In such cases the Income-tax Officer may consider it advisable to issue a notice under section 22 (4) calling for accounts and another under section 23 (2), requiring the assessee to produce such evidence as he desires to adduce in support of his return. It is to be observed that a notice under section 23 (2) is in the interests of the assessee and must be issued; while one under section 22 (4) may or may not be issued according as the Income-tax Officer may or may not deem it expedient having regard to the cir-

cumstances of the case, but if issued must be obeyed. The plain language of the sections enables one to arrive at the result indicated above. It is, however, pointed out that section 37 of the Income-tax Act empowers the Income-tax Officer to direct the production of documents by any person, assessee or otherwise, in the manner laid down by the Code of Civil Procedure in relation to suits and proceedings before civil courts, and it is argued that after an enquiry initiated by section 23 (2) has commenced, the production of accounts is to be enforced not by a resort to a notice under section 22 (4) but by the exercise of the power conferred by section 37. It may be that the law has provided more than one mode of securing evidence, but because an alternative method of achieving a certain object is available it does not follow that another, if it is otherwise permissible, should be denied. There is a difference between the provision contained in section 22 (4) and that laid down in section 37. The latter applies to assesseees and others in a position to give evidence, while the former which is more drastic, is applicable only to assesseees who are to be visited with certain consequences in case of failure to produce accounts.

Reliance has been placed on a case decided by a Division Bench of the Lahore High Court, *Khushi Ram Karam Chand v. Commissioner of Income-tax, Punjab*(1). It does support the contention of the assesseees in the case before us. The reasons given by the learned Judges for not giving effect to the plain language of section 22 (4) are thus stated by them:—"The words 'having made a return' and the order in which the defaults are enumerated in section 23 (4) indicate that a notice under section 22 (4) precedes the notice and enquiry under section 23. It is significant that sub-section (4) section 23 does not authorise a summary assessment in the case of a default under section 23 (3)". The learned Judges also observed that "It is true that the wording of section 22 (4) is somewhat wide, but it must be construed with reference to the context. It is also a well established rule of the interpretation of fiscal enactments that, in case of doubt, an interpretation which is more favourable to the subject is to be preferred."

With great respect to the learned Judges I am unable to agree with this view. The order in which certain provisions occur may in some cases assist us in construing one of those provisions. But where the arrangement is consistent with a reading which gives effect to the entire language of that provision, its plain meaning cannot be departed from only because a different location of such provisions would have made that meaning clearer. The reason why the provision in question before us has been made sub-section (4) of section 22 and placed before the enquiry provided for by section 23 (2) is that ordinarily notice under the former will precede the notice contemplated by the latter. Assuming for a moment that the Legislature intended to confer a power on the Income-tax Officer to issue a notice non-compliance with which should attract the operation of section 23 (4), whether such notice is issued before or after the commencement of the enquiry, where is the provision to be inserted? If it be placed between sub-sections (2) and (3) of section 23 to make it plain that such notice can be issued after the commencement of the enquiry it would lead to the result, according to the reasoning based on the order of the provisions, that the Income-tax Officer has no power to issue such a notice before the commencement of the enquiry. It follows, therefore, that the arrangement of the provisions is not a safe guide in this particular instance. It is not disputed that the language of section 22 (4) is wide enough to enable the Income-tax Officer to issue before the commencement of the enquiry a notice under section 22 (4) which if disobeyed will entail the consequences mentioned in section 23 (4).

The words "having made a return" occurring in section 23 (4), founded on in the ruling referred to, do not, in my opinion, support the conclusion arrived at in that case. These words may possibly make it arguable that notice under section 22 (4) can be issued only where a return has not been made, an argument which I have already disposed of. The learned Judges who decided that case do not seem to be inclined to accept it, and on the contrary are of opinion that section 22 (4) "is apparently intended to help the Income-tax Officer in deciding whether he will accept the return or proceed to make any enquiry." It seems to me that the words "having made a return" in section 23 (4) have been used because section 23 (2) to which they relate presupposes that a return has been made. In cases to which section 22 (1) and (2) apply, return is out of question; while in cases to which section 22 (4) applies, return may or may not have been made. The object of introducing these words in relation to section 23 (2) is to indicate what is certain to have happened, unlike the preceding two cases in which a return *might or might not* have been made. They cannot be so read as to imply that in the first two cases return *could not* have been made. I have already pointed out one of the objections to such a construction, viz., that we in effect, insert some such words as "and who has not made the return" after sub-section (2) in section 22 (4) which is more vicious than treating the words "having made the return" in section 23 (4) somewhat lightly. The view taken by the learned Judges of the Lahore High Court is diametrically opposed to what has been held by at least three High Courts: in *Charāra Sen Jaini v. Commissioner of Income-tax, U. P.*(1), in *Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal*(2), and in *Ram Khehwan Ugam Lal v. Commissioner of Income-tax, Behar and Orissa*(3). It has been distinctly ruled that notice under section 22 (4) may be issued at any time before or after the commencement of an enquiry contemplated by section 23 (2), and that the words "having made a return" occurring in section 23 (4) do not signify anything which may affect the plain language of section 22 (4).

For the reasons detailed above I answer the first question in the affirmative.

The second question runs thus:—“(2) Was the notice under section 22 (4) issued by the Income-tax Officer, Cawnpore, on February 22, 1928, invalid, because it included accounts and documents connected with the Calcutta shop?” That the Income-tax Officer of Cawnpore had jurisdiction to assess tax on the income derived by the assessee from the Calcutta branch of their business is not disputed, and in view of the provisions of section 64 of the Income-tax Act such jurisdiction cannot be denied. This being so, it can scarcely be maintained that a notice issued under section 22 (4) calling upon the assessee to produce or cause to be produced their accounts of the Calcutta branch is invalid. It was certainly open to the Income-tax Officer, Cawnpore, to require the Income-tax Officer, Calcutta, to send the account books which appear to have been produced before him by the assessee who were for some reason of their own reluctant to have such accounts subjected to the scrutiny of the Income-tax Officer, Cawnpore. The latter preferred to make the assessee responsible for the production of these accounts and whether he was right or not in the exercise of his power to adopt the more drastic of the two courses open to him he cannot be said to have done what he had no jurisdiction to do. It has been contended that the Income-tax Officer, Cawnpore, having called for a report from the Income-tax Officer, Calcutta, regarding the income of the assessee accruing there, he (the Income-tax Officer, Cawnpore), ceased to have jurisdiction in regard to that matter. I cannot accede to this contention. It is only a departmental arrange-

(1) 3 I. T. C. 17.

(3) 3 I. T. C. 225.

(2) 3 I. T. C. 198.

ment that one Income-tax Officer requires another to furnish information on matters supposed to be better known to him; but in doing so he does not divest himself of the powers which the law has conferred on him, so as to become *functus officio*. My answer to the second question is in the negative.

The opinion of the Commissioner on the third and fourth questions has not been challenged by the learned Advocate for the assessee, and I think rightly. I answer them in the negative.

The fifth and sixth questions have been argued together and may be so disposed of. They are as follows:—(5) Was the Income-tax Officer entitled, in the face of the statement of Pandit Sheo Nath Pandey, the assessee's mukhtar-i-am, dated March 14, 1928, to hold that the notice under section 22 (4), dated February 22, 1928, had not been complied with? (6) When an assessee denies the existence of accounts or documents, may the Income-tax Officer presume the existence of such accounts or documents? Where the Income-tax Officer has reason to believe that certain accounts and documents are in the possession or power of the assessee and calls upon him under section 22 (4) to produce them, but the assessee denies the existence of such documents, the Income-tax Officer can arrive at his own conclusion in view of the circumstances of the case, and if he persists in his belief that such accounts and documents exist and ought to have been produced, he can proceed under section 23 (4). The assessee has a remedy by challenging the finding of the Income-tax Officer under section 27 of the Income-tax Act which provides that "Where an assessee within one month from the service of a notice of demand.....satisfies the Income-tax Officer.....that he did not receive the notice issued under sub-section (4) of section 22,..... or that he had not a reasonable opportunity to comply, or was prevented by sufficient cause from complying, with the terms of the last mentioned notices, the Income-tax Officer shall cancel the assessment and proceed to make a fresh assessment in accordance with the provisions of section 23". From the finding arrived at by the Income-tax Officer under section 27 adversely to the assessee an appeal has been allowed by section 30 of the Act and if he satisfies the appellate authority that he was prevented from complying with the notice under section 22 (4) because the accounts and documents to which it related did not exist, he will escape the consequences of his regarding that notice. It must be conceded that the procedure laid down for an assessee, who is believed to possess certain accounts and documents, to vindicate his denial in that respect, is clumsy and one-sided, but such appears to be the law as it stands. I answer the fifth and sixth questions in the affirmative.

The seventh and eighth questions may be disposed of together. They are as follows:—(7) Has the Income-tax Officer of an assessee's principal place of business jurisdiction to compel such assessee to submit a return and produce accounts in respect of a branch business when he has submitted a return, produced accounts, and otherwise complied with all the requirements of the law before the Income-tax Officer of the place where he has such branch business? (8) Is the Income-tax Officer of the principal place of business bound to accept the report of the Income-tax Officer of a place where an assessee is carrying on a branch business? If not, is he bound to refer the matter back to the latter officer for further enquiry and not to assess according to his judgment? My remarks in answering the second question have a bearing on the questions and should be referred to. As stated by me in that connection the Income-tax Officer, Cawnpore, which is the principal place of the business of the assessee, had jurisdiction to assess the tax on their income from all sources. It follows that he could and to direct the production of accounts thereof. The assessee is not relieved

of the obligation imposed on them by making a return of their income derived from a branch concern to the Income-tax Officer of the district where such branch concern is carried on and by producing accounts relating thereto before such officer. The law gives to the assessee no choice in this matter. I answer the seventh question in the affirmative and the eighth in the negative.

The ninth question as it stands is too widely put. It runs thus:—(9) In all the circumstances of this case, was the assessment rightly made under section 23 (4). Taking it as it stands the language would include the question whether the Income-tax Officer was right in the exercise of his *discretion* to proceed under section 23 (4) or under section 23 (3). But I think the learned Commissioner making the reference meant no more than to obtain a ruling of this Court on the question whether under the circumstances of this case the Income-tax Officer, Cawnpore, had jurisdiction to make an assessment under section 23 (4). For the reasons which I have already stated in answering question No. 1. I would answer the ninth question in the affirmative.

BY THE COURT:—As we are not agreed as to our answer on question No. 1, we refer the “case” under Sec. 98, C.P.C. and Sec. 66 (2) of the Income-tax Act, 1922, to the Hon’ble the Chief Justice, for orders as to it being put before a Single Judge or a Bench of Judges, as he may think fit. We, however, want to mention that the question is of utmost importance to the Income-tax authorities and the public who pay the tax, that, on the point, different High Courts have taken different views and that it might be desirable to require a Bench of 3 Judges to hear the point and decide it, to avoid a further difference of opinion, and a second reference.

The question No. 1 is as follows:—Has an Income-tax Officer jurisdiction to issue a notice under Sec. 22 (4) after the commencement of an enquiry under section 23 (3)?

OPINION.

BOYS, KENDALL AND YOUNG, JJ.:—This is a reference under Sec. 98 of the Code of Civil Procedure made by a Division Bench of this Court in a matter arising under the Income-tax Act of 1922. Notice was served on Lachhman Das Babu Ram a firm with their head-quarters at Cawnpore and branches in other places, under Sec. 22 (2) of the Income-tax Act to make a return of their income. After certain proceedings, which it is unnecessary to detail, a combined notice was sent to the firm on August 11th, 1927, in the form known as Form B, drafted apparently under the authority of the Board of Revenue but not incorporated in any way in the Income-tax Act. This so-called combined notice purports to be a notice under Sec. 22 (4) and also under Sec. 23 (2) of the Act. The nature of the notices that can be issued under those two sections is clear on the face of the sections themselves and we need not detail it. After many postponements and the receipt of many reports and the examination of certain accounts, next on the 22nd of February, 1928, the Income-tax Officer felt that he had reason to ask for further particulars in regard to the purchase of a house, and issued what we are told was a notice under Sec. 23 (3) asking for particulars in regard to this house. In the statement of the case made by the Income-tax Commissioner this notice is referred to as having been one under Sec. 23 (2) but that is apparently a misprint, and this notice of February 22nd 1928, was presumably a notice asking for evidence on “specified points” in accordance with sub-section (3) of Sec. 23. On the same date, February 22nd he issued another notice under Sec. 22 (4) calling for certain Cawnpore head-quarters accounts. On the 14th of March 1928, one Sheonath was examined on oath and this appears

to be the only occasion on which any "evidence" was heard. On the 30th of March, after certain reports had been received, the Income-tax Officer asked for further accounts. The representative of the firm asked for a further reference to the Calcutta branch, but this was refused as the day, March 30th, was the last day but one for the close of the financial year, and the Income-tax Officer proceeded to a summary assessment, purporting to act under Sec. 23 (4). Upon the assessee appealing to the Assistant Commissioner it was held that he had no right of appeal owing to the fact that the assessment had been made and properly made under Sec. 23 (4). The assessee thereupon required the Income-tax Commissioner to refer the case to this Court on certain points stated. A number of those points came up for consideration before a Bench of this Court consisting of Mr. Justice Mukerji and Mr. Justice Niamat Ullah. On one point the learned Judges have differed, and the matter has come up before the present Bench of three Judges on the reference. The point referred to us is stated by the learned Judges as follows:—"Has an Income-tax Officer jurisdiction to issue a notice under Sec. 22 (4) *after the commencement of an inquiry under Sec. 23 (3).*"

We have had some difficulty in ascertaining the facts on the basis of which we are asked to decide this question. The following appears in the statement of the Income-tax Commissioner:—"The assessee now desire that I should make a reference to the Hon'ble High Court on the following points of law (Appendix E) (as propounded by them); (a) Whether the notice issued under section 22 (4) on February 22, 1928, was legally valid inasmuch as it was issued after the commencement of proceedings under Sec. 23 (3);" etc.

It does not appear, however, that we have to consider the effect of the notice on February 22nd, 1928, at all. The notice under Sec. 22 (4) which we have really to consider, is referred to in the Income-tax Commissioner's statement at paragraph 20, point 9. It is referred to us as follows: "The assessee clearly failed to comply with the notice under section 22 (4) issued on August 11, 1927 calling for the production of their Calcutta accounts. This default justifies the assessment under Sec. 23 (4)". The Assistant Commissioner also said in his order, dated June 15th, 1928, which is printed as Appendix D to the Income-tax Commissioner's statement of the case: "and there was the failure to produce the Calcutta accounts for which a notice was issued on August 11th, 1927. These circumstances clearly reduce the assessment to one under section 23 (4)." A consideration of the facts chronologically set out at the commencement of this judgment will show that no inquiry under Sec. 23 (3) commenced until the date of the 14th of March 1928, when the evidence of the one witness Sheonath was heard on oath. It is manifest therefore that neither the notice issued on the 11th of August 1927, nor that issued on the 22nd of February 1928, was issued after the commencement of the inquiry under Sec. 23 (3). The question, therefore, which has been referred to us does not appear to us to arise on the facts of the case. We may add that Mr. Bajpai, the Government Advocate who has represented the case here for the Crown, has had the advantage of the presence of the Income-tax Officer in Court assisting him in the case, and Mr. Bajpai himself, after having consulted the Income-tax Officer, agrees that no inquiry under Sec. 23 (3) can be said to have commenced until the 14th of March 1928. Even if it could be said to have commenced on the 22nd of February 1928, the date on which a notice was issued under Sec. 23 (3) to produce evidence as regards the specified point of the purchase of a house, a point which we have not to decide, it is manifest that the notice under Sec. 22 (4) of the 11th of August 1927, was long prior to that date.

We, therefore, direct that this case be returned to the Bench that referred it to us, with the expression of our opinion that the point referred to us does not on the facts of the case arise.

FINAL JUDGMENT.

MUKERJI, J.:—By an order of this Bench dated the 2nd of February, 1929 we directed that the matter in difference between the Judges composing this Bench might be referred to a single Judge or a Bench of three Judges. The Hon'ble the Chief Justice was pleased to appoint a Bench of three Judges. The matter was considered by the learned Judges to whom the matter in difference between us was referred. The learned Judges came to the conclusion that in the circumstances of the case, the question referred to, namely, the question No. 1 of the nine questions referred to the High Court by the Commissioner of Income-tax did not arise. This Bench thought that the learned Judges who expressed the opinion quoted above were not authorised under the provision of law under which the reference was made to say that the question did not arise. This Bench accordingly addressed the learned Chief Justice again proposing that the said question No. 1 might again be referred to other Judges. The learned Chief Justice thereupon called a meeting of the Judges of the Court and the majority of the Judges decided that it was open to the three Judges, to whom the question had been referred, to say that the question did not at all arise and that such opinion would be binding on the division Bench which referred the question.

The matter was again placed before us. We have heard the counsel for the parties. Dr. Katju has argued that on the judgment delivered by the three learned Judges mentioned above the answer to the question No. 9 as recorded by us previously should be reconsidered. He has argued and in my opinion quite correctly that question No. 9 and question No. 1 are not identical. The question No. 1 is 'Has an Income-tax Officer jurisdiction to issue a notice under Sec. 22 (4) after the commencement of enquiry under Sec. 23 (3)?'. The question No. 9 runs as follows: 'In the circumstances of this case, was the assessment rightly made under Sec. 23 (4)?'

Question No. 1 is a pure question of law and on this point my brother Niamat Ullah, J., and I are at a difference. Dr. Katju argues that in spite of this difference, we ought to say in answer to question No. 9 that having regard to the facts of the present case the assessment was *not* rightly made under Sec. 23 (4).

Let us examine the contention of Dr. Katju. He has pointed out that when the Income-tax Officer at Cawnpore started his enquiry, he asked for the account books from all the places of business from the assessee, namely, from Cawnpore, from Bombay and from Calcutta. The Bombay and Cawnpore accounts were produced but the Calcutta accounts were not produced before the Officer at Cawnpore. The Income-tax Officer at Cawnpore issued a notice on 11th August 1927 which was a combined notice under Secs. 23 (2) and 22 (4) of the Income-tax Act, to produce the Calcutta accounts on 15th August. To this order the assessee demurred and requested the Income-tax Officer at Cawnpore not to press his order but to allow them to produce their accounts before the Income-tax Officer at Calcutta. To this request the Officer at Cawnpore acceded. He wrote to the Officer in Calcutta as follows (see p. 9, Appendix A); 'It is therefore the Calcutta shop account which is the most important. I would request you to examine these books again and obtain copies. I would have taken all this trouble on myself but the assessee is unwilling to show the Calcutta shop accounts to me. The case is important and requires your per-

sonal attention. I have fixed the case for March the 6th, 1928, and shall be extremely obliged to have your reply before that date."

This letter was written as late as on February 24th 1928, and evidently after some other correspondence had passed, Dr. Katju urges and in my opinion rightly, that by agreeing to accept the report of the Income-tax Officer, Calcutta, provided the same was satisfactory, the Officer in Cawnpore, waived, so to say, the effect of his order dated the 11th August 1927. That order, argues Dr. Katju, could not be revived after seven months in March 1928, and could not be made the basis of an order under Sec. 23 (4) of the Income-tax Act, namely an assessment to the best of the judgment.

It will be remembered that there were two notices issued against the assessee, both purporting to be combined notices under Secs. 22 (4) and 23 (3); one was dated the 11th August 1927, and the other was dated the 22nd February 1928. It was on account of the failure to comply with both these notices, that the Income-tax Officer purported to act under Sec. 23 (4) of the Income-tax Act. When the assessee questioned the propriety of this assessment "to the best of judgment" they questioned the validity of the notice of 22nd February 1928: See point (a) at p. 3 of the statement of the case. The learned Commissioner is required by law to give his own opinion on the points referred to the High Court for its opinion. In answering the question No. 9 (see p. 8 of the statement of the case) the learned Commissioner did not rely on the notice issued on 22nd February 1928, but relied on the notice of 11th August 1927 only. For this reason the Bench consisting of three learned Judges of this Court expressed the opinion that the notice of 22nd February 1928 might very well be ignored. The learned Judges then considered the circumstances under which the notice of 11th August 1927 had been issued and came to the conclusion that it had been issued before any enquiry was started. From this finding of fact it followed that the question of law on which there was a difference of opinion between myself and my learned brother did not arise. Dr. Katju has argued that if we are bound by the opinion of those three learned Judges, as the majority of the Judges of the Court have held in an English Meeting, we must ignore the notice of 22nd February 1928, as being a document of no relevancy in the case.

In my opinion, this view contended for ought to be accepted and for the reasons already given. Further, however, there is good reason why the notice of 22nd February 1928 should be ignored as waived or as being never intended to be operative. I have already pointed out that the letter addressed by the Income-tax Officer of Cawnpore to the Income-tax Officer at Calcutta is dated the 24th February 1928, (see Appendix A) and was therefore written two days after the notice dated the 22nd February 1928, had been issued. From the portion of the letter quoted above it will be seen that the Income-tax Officer at Cawnpore was perfectly willing to accept the report of the Calcutta Officer and it was not his intention to enforce either the notice of 11th August 1927, or that of 22nd February 1928.

Whether we accept the opinion of the Full Bench or whether we decide on our own initiative, there can be no doubt that both the combined notices had been waived so to say, and it would be extremely unfair on the part of the Income-tax Officer to turn round and say, without giving the assessee a fresh opportunity to produce the books, that their failure on previous occasions to produce accounts subjected them to the penalty of having a best judgment assessment made against them.

In view of this fresh argument and in view of the opinion expressed by the Full Bench I am clearly of opinion that the answer to question No. 9 should be in the negative.

I may point out that this answer entirely makes it unnecessary to return any answer to question No. 1 and as already stated in the opinion of the Full Bench, the question No. 1 does not arise.

I would therefore direct that, in substitution of my answer to question No. 9 as recorded on 22nd February 1928, the detailed answer which is also in the negative recorded above be returned to the Commissioner of Income-tax.

I note that Mr. Bajpai the learned Government Advocate has argued in Court for 4½ days and that he is entitled to a fee of Rs. 1,100. He should get this fee from the Government. As regards the costs of this reference, I would direct that the Government should pay the costs of the assesseees.

NIAMAT ULLAH, J.:—In my order of 22nd February 1929, I answered the question No. 9 in the affirmative, because, in my view, disregard of a notice under section 23 (2) of the Income-tax Act entitles the Income-tax Officer to proceed under section 23 (4) and if he does so, the assessee has no right of appeal. Whether the Income-tax Officer could do so under the circumstances of the present case depended on the effect of two notices issued by him (1) on the 11th August 1927, and (2) on the 22nd February 1928. It had been contended on behalf of the assesseees that the first notice had been waived. I did not deal with this argument, because if it be accepted with regard to the first, the second notice, which in my opinion cannot be said to have been waived as the result of a letter, dated the 24th February 1928, could not be got over. I would have respectfully differed from my learned colleague on this part of the case, had the question been open to discussion; but the view taken by the Full Bench, as regards the second notice relieves me of the responsibility of dealing with it. The Full Bench have placed their own construction on the statement of facts submitted by the Income-tax Commissioner, according to which the effect of the notice dated the 22nd February 1928, is not to be considered. They observed, after considering the statement of the case, that "it does not appear, however, that we have to consider the effect of the notice on February 22, 1928 at all". As regards the first notice, they ruled that it was issued before the commencement of the enquiry, in which case, according to the view both of my brother Mukerji, J., and myself, the Income-tax Officer had jurisdiction to proceed under section 23 (4), unless he is otherwise debarred from taking that course. On receipt of the finding of the Full Bench, the assesseees pressed for the consideration of the question that the first notice (of 11th August 1927) had been waived. The second notice (of 22nd February 1928) being ignored, as we must ignore in view of the ruling of the Full Bench, I must now consider the effect of the former. I have had the advantage of reading the judgment of my learned colleague, and find myself in agreement with him in holding that, under the circumstances of the case stated by him, it was waived with the result that it loses its legal effect altogether.

In accordance with the views expressed by the Full Bench and for the reasons stated above, I have to answer question No. 9 in the negative, which I accordingly do.

BY THE COURT:—Let the following answers to the questions put by the Commissioner of Income-tax be returned as the answers of the Court. Along with the answers will be sent copies of all the judgments of the Judges forming this Bench and the Judges forming the Bench to which the question No. 1 was referred for an answer. Question No. 1. In the view expressed by the Bench of three Judges this question does not arise.

Question No. 2	Answer	No.
Question No. 3 (a)	"	"
" No. 3 (b)	"	"
" " 4	"	"
" " 5	"	Yes.
" " 6	"	"
" " 7	"	"
" " 8	"	No.
" " 9	"	"

With reference to the costs we declare that the Government Advocate having worked for more than 4 days is entitled to a fee of Rs. 1,100. As the assessee has substantially succeeded in the reference, we direct that he shall get his costs from the opposite party.

(319) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Sir Benjamin Heald, Kt., Chief Justice and Mr. Justice Maung Ba.

(16th July, 1929).

P. K. N. P. R. Chettyar Firm

.. Assessee.*

v.

The Commissioner of Income-tax, Burma.

Indian Income-tax Act (XI of 1922), Secs. 23 (4) 27, 33 and 66 (2) and (3)—Assessment to the best of judgment—Scope and limits of Income-tax Officer's powers—Arbitrary assessment,—Revision under Sec. 33—Sufficiency of cause under Sec. 27—If a question of law for reference.

The question of sufficiency of cause under section 27 of the Income-tax Act involves the question whether judicial discretion has been exercised in a sound and reasonable manner, or has been exercised capriciously, arbitrarily or in a judicially unsound manner and hence is a question of law within the meaning of Sec. 66 (2) and (3) of the Income-tax Act.

An assessment under Sec. 23 (4) must be made according to rules of reason and justice, not according to private opinion, according to law and not humour and the assessment must not be arbitrary, vague and fanciful but legal and regular.

An assessment not purporting to be based on the admittedly available materials or any materials at all beyond the Income-tax Officer's mere whim or humour cannot be regarded as an assessment in respect of which the discretion given to the Income-tax Officer under section 23 (4) has been properly exercised and the Commissioner ought to exercise the discretion given to him under Sec. 33 in respect of such an assessment.

Application [Civil Miscellaneous Application No. 10 of 1929] under Sec. 66 (3) of the Indian Income-tax Act, (XI of 1922), for an order to direct the Commissioner of Income-tax, Burma, to state a case for the opinion of the High Court.

Hay and Venkataraman, for the Assessee.

Gaunt, for the Crown.

* A. I. R., (1930) Rang. 82.

JUDGMENT.

Applicants, who are the P. K. N. P. R. Chettyar firm, returned an income of Rs. 34,000 for assessment of income-tax for the year 1927-28, but in their return they did not give all the details required by section 22 (2) Income-tax Act, their agent alleging that he was not in a position to give such details. They were given notice under section 22 (4) to produce their accounts and they produced what they alleged to be the complete set of their account books. They did not produce what are known as "Baki" books and their agent swore that they did not keep such books. The Income-tax Officer came to the conclusion that they did keep such books, and on the footing of their default in respect of their return under section 22 (2) and also in respect of their account books under section 22 (4) proceeded to make an assessment under section 23 (4) and assessed applicants on an income of Rs. 1,25,000.

Applicants filed an application under section 27, asking that the assessment should be cancelled and that a fresh assessment should be made. They said that their failure to give the required details in their return under section 22 (2) was due to the fact that that return had to be made at a time when in the usual course of their business their accounts for the year 1926-27 had not been closed, that they followed the usual practice of Chettyar Firms in such cases by producing all their books before the Income-tax Officer, and that in fact they did not keep "Baki" books. They claimed that in the circumstances they had not made any default under section 22 (2) or section 23 (2) or section 22 (4) and the assessment made by the Income-tax Officer under section 23 (4) should be cancelled and a fresh assessment should be made under the provisions of section 23. The Income-tax Officer said that, whatever the practice of appellants' business might be, they could not evade the obligation of filing a statement showing details of the receipts and expenditure on which they based their return under section 22 (2) and that he was still convinced that they did in fact maintain "Baki" books. He, therefore, rejected their application under section 27.

Applicants appealed to the Assistant Commissioner under section 30 (1) against the Income-tax Officer's refusal to make a fresh assessment under section 27 alleging that they had produced all their books and that in the circumstances of the case their failure to file a statement of receipts and expenditure for 1926-27, did not amount to default under section 22 (2) of the Act. They said that the Income-tax Officer had disregarded the facts that they had produced all their books and that in the two previous years they had been assessed on an income of Rs. 50,000 or Rs. 60,000, that these facts should be taken into consideration, that the assessment should have been based on their books which in fact showed their actual income for 1926-27 and that the Income-tax Officer's action in assessing them on an income of Rs. 1,25,000 was entirely arbitrary.

The Assistant Commissioner found that applicants did not in fact keep "Baki" books and that they had actually produced all their account books, but he said that they were in default in that they had failed to file a statement of their receipts and expenditure for 1926-27 and that, therefore, the Income-tax Officer was entitled to make an assessment to the best of his judgment under section 23 (4) and was justified in refusing to cancel the assessment under section 27. Applicants then applied to the Commissioner to refer certain questions to this Court under section 66 (2) and they also asked him to review the order of the Assistant Commissioner under section 33. The Commissioner agreed with the Income-tax Officer and the Assistant Commissioner that applicants had not in fact complied with the provisions of section 22 (2) and he said that by reason

of that default no question of law arose as to the power of the Income-tax Officer to make an assessment under the provisions of section 23 (2). He said further that because no appeal lies against such an assessment the only questions which were before the Assistant Commissioner on an application under section 27 were the questions mentioned in that section, namely, whether the applicants were prevented by sufficient cause from complying with the terms of those notices, and that, so far as the Assistant Commissioner was concerned, the question whether or not the Income-tax Officer had in fact used his best judgment or had made the assessment arbitrarily did not arise. He, therefore, refused either to make a reference to this Court or to review the Assistant Commissioner's order. Applicants now ask us to direct the Commissioner to refer the case to this Court under the provisions of section 66 (3).

The scheme of the Act is apparently that if in fact an assessee fails to make a return in the terms of the form prescribed under section 22 clause (2), or if he fails to produce such accounts or documents as the Income-tax Officer may require under section 22 (4), or if he fails to produce evidence under section 23 (2), then unless he can show that he was prevented by sufficient cause from making the return or that he did not receive the notices under section 22 (4) or section 23 (2) or that he had not a reasonable opportunity to comply or was prevented by sufficient cause from complying with those notices, he is liable to be assessed under section 23 (4) "to the best of the Income-tax Officer's judgment", that there shall be no appeal against such an assessment and that the only remedy against an arbitrary assessment, that is, against what is in effect a fine of unlimited amount, shall be the discretion of the Commissioner to review the assessment under section 33.

But when section 23 (4) says that the Income-tax Officer "shall make the assessment to the best of his judgment" it means that he must make it "according to the rules of reason and justice not according to private opinion, according to law and not humour," and that the assessment is to be "not arbitrary, vague and fanciful, but legal and regular". In cases where the assessee has admittedly filed complete accounts and there is no suggestion that these accounts are false or fraudulent and where there are available the actual assessments for previous years, which may be presumed to have been regularly and properly made, an assessment which should have been made, "to the best of the Income-tax Officer's judgment" but which does not even purport to be based on the materials which were admittedly available or on any materials at all beyond the Income-tax Officer's mere whim or humour, can hardly be regarded as an assessment in respect of which the discretion given to the Income-tax Officer by section 23 (4) has been properly exercised, and is in our opinion an assessment in respect of which the Commissioner ought to have exercised the discretion given to him by section 33.

But our opinion that the Commissioner has failed in his duty under section 33 will not give us jurisdiction to require the case to be referred under section 66, sub-section (3) of the Act, since that sub-section relates back to sub-section (2) and sub-section (2) deals only with orders made under section 31 or section 32 and not with orders made under section 33. What we have to decide is whether or not a question of law arises out of the Assistant Commissioner's order under section 31, that order being made an order made in an appeal against an order under section 27.

Section 27 says that if the assessee "satisfies" the Income-tax Officer that he was prevented by sufficient cause from making the return required by section 22 or from complying with the terms of notices issued under section 22 (4) or section 23 (2), the Income-tax Officer shall cancel the assessment. The

words "satisfies" and "prevented from sufficient cause", are similarly used in rule 9, Order 9, Sch. 1, to the Civil Procedure Code, and in section 5, Limitation Act, the corresponding words in rule 19 of Order 41, being "it is proved" and "prevented by a sufficient cause". All these provisions of law have been interpreted as importing a discretion, and since the words "satisfies the court" simply mean "proves", it would appear that the discretion lies in the power to determine whether or not the cause shown is "sufficient". The question of sufficiency of cause seems thus to have been regarded differently from the question of sufficiency of evidence, since it has always been held that the determination of sufficiency of cause involves the question whether the judicial discretion has been exercised in a sound and reasonable manner or has been exercised capriciously, arbitrarily or in a judicially unsound manner so as to involve a question of law. The Income-tax Officer undoubtedly had such a discretion under section 27 and the Assistant Commissioner had a similar discretion in an appeal from an order under that section.

We hold, therefore, that a question of law, namely, whether or not the discretion given by section 27 was properly exercised arises out of the Assistant Commissioner's order under section 31, and, therefore, under section 66 (3) we require the Commissioner to state the case and to refer it to this Court. The costs in respect of this application will abide the final order for costs which will be made on the reference.

(320) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice Fazl Ali, and Mr. Justice Chatterji

(19th July, 1929).

Firm of Mohan Lal Hardeo Das Assesseees
vs.

The Commissioner of Income-tax, Bihar and Orissa

Indian Income-tax Act (XI of 1922) Secs. 22 (4), 23 (2), 30 and 66 (2) and (3)—Limitation for reference applications—Starting point—Exclusion of time in obtaining copy—"Passing of the order", meaning of—Notice to produce evidence—Assessment under Sec. 23 (4) on non-compliance—Appeal against assessment—Amendment of demand notice, if invalidates appeal.

The expression "passing of the order" in Sec. 66 (2) of the Income-tax Act cannot be interpreted as the communication of the order to the party and time runs from the date of recording of the order under Secs. 31 or 32 of the Act.

In computing the period prescribed by Sec. 66 (2) and (3) of the Act, on general principles and in view of Sec. 29 of the Limitation Act, an assessee is entitled to deduct the time spent in obtaining a copy of the order with which he is dissatisfied.

Where the assesseees called upon under Secs. 22 (4) and 23 (2) to produce their account books and any evidence in support of their return neither appeared nor produced the accounts or any evidence but requested the Income-tax Officer to assess on the materials already before the Officer,

HELD, that an assessment under Sec. 23 (4) was properly made.

Non-production of any evidence in support of the return called for by notice under Sec. 23 (2) would amount to failure to comply with all the terms of the notice within the meaning of Sec. 23 (4) of the Act.

OBITER. An appeal under Sec. 30 of the Act is against the assessment and not against the demand notice and the Assistant Commissioner would have no power to throw out an appeal merely because the demand notice was subsequently amended by the Income-tax Officer.

Application [Miscellaneous Judicial Case No. 56 of 1929]. under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the the Commissioner of Income-tax, Bihar and Orissa, to state a case for the opinion of the High Court.

Hasan Jan and Ahmed Reza, for the assesseees.

Agarwala, for the Crown.

JUDGMENT.

FAZL ALI, J.:—This is an application asking us under section 66 clause 3 of the Income-tax Act to call upon the Income-tax Commissioner to draw up a statement of the case and refer it with his own opinion to this Court.

The petition is on behalf of a firm carrying on business in the districts of Monghyr, Darbhanga and Calcutta. The firm was called upon to submit a return in respect of its income for the years 1923 and 1924 and to file account books. The Income-tax Officer of Calcutta found that the business in Calcutta had suffered a loss of Rs. 14,725 while the Income-tax Officers of Darbhanga and Monghyr found that the firm had made a profit of Rs. 8,500 and 8,000 respectively in those districts. The Income-tax Officers of Calcutta and Darbhanga also reported the result of their examination of the accounts produced by the petitioners to the Income-tax Officer of Monghyr. The Income-tax Officer of Monghyr then proceeded to assess the petitioner upon a total income of Rs. 22,000. On the 29th June 1924 the Assistant Commissioner cancelled the assessment and directed a fresh assessment. Between this date and now the case has had, to use the words of the Income-tax Commissioner, "a long and muddled history" for which some of the orders passed by the officers of the Income-tax Department are to some extent responsible.

It will suffice, however, for the purpose of considering the present application not to go further back than the order passed by the Commissioner of Income-tax on the 15th December 1927. By this order he directed the Income-tax Officer to make a fresh assessment for the years 1923 and 1924 after calling for the accounts of the business in Calcutta and Monghyr. In pursuance of this order the income-tax Officer of Monghyr issued a notice on the 19th January 1928 under section 22 clause 4 and section 23 clause 2 calling for the books of account referred to in the order of the Commissioner and fixing 8th February 1928. On that date a petition was received by registered post by the Income-tax Officer in which it was stated that the account books had been destroyed and the assessee could not produce them. It may be mentioned that the case of the petitioners as put forward before us, is that the books were sent to Marwar where they were eventually destroyed by whiteants. The case was then postponed till the 27th February 1928 on which date the firm was asked to produce any other evidence it chose in support of the return. No one appeared on that date but a petition was received in the office on the 28th February 1928 in which the petitioner stated that the firm had no further evidence to rely on than the findings of the Income-tax Officers of all the three places which were already before the Income-tax Officer of Monghyr. The Income-tax Officer then proceeded to assess the petitioners estimating the income once more to be Rs. 22,000. The petitioners thereupon appealed to the Assistant Commissioner of Income-tax and it appears that while the appeal

was pending, the Income-tax Officer finding that the demand notice was not quite regular cancelled it under section 35 and issued a fresh demand notice showing that the assessment had been made under section 23 clause 4. Sometime later the Assistant Commissioner of Income-tax heard the appeal which was disposed of by an order dated the 5th July 1928. The latter part of the order passed by the Assistant Commissioner of Income-tax shows that he rejected the appeal mainly on the ground that the notice of demand which had been originally issued by the Income-tax Officer having been cancelled and rectified under section 35 and there being no appeal against the "rectified notice" which was issued after the appeal before him had been filed, the appeal was not maintainable. It appears that an intimation of the order passed by the Assistant Commissioner was sent by post to the petitioners on the 7th July 1928 and it reached them sometime after the 8th July 1928. The petitioners thereupon sent a petition to the Commissioner of Income-tax asking him to refer certain questions of law to the High Court along with a statement of the case as well as his opinion thereon. This application was disposed of by the Commissioner of Income-tax on the 20th December 1928, one of the grounds being that the application was out of time. The petitioners thereupon filed this petition before this Court on the 24th June 1929.

Now, the learned Counsel who appears for the Income-tax Department raises certain preliminary objections and asks us to hold that this petition is not maintainable. His first contention is that the application was not thrown out by the Commissioner of Income-tax on the ground that no question of law arose but on the ground that the application was out of time and this being so, the requirements of section 66 clause 3 are not fulfilled in this case and this Court is not competent to proceed under section 66 clause 3. The simple reply to this point, however, is that the Commissioner has elaborately dealt with the points of law raised by the petitioners in their application before him and the order passed by him makes it absolutely clear that he has refused to state the case not only on the ground that the application before him was out of time, but also on the ground that no question of law arose in the case.

The next point raised by the learned Counsel for the Income-tax Department was that the applications before the Commissioner of Income-tax as well as before this Court are out of time. It will be necessary here to refer to a few dates in order to appreciate the point raised by the learned Counsel. As I have already stated the Assistant Commissioner of Income-tax rejected the petitioner's appeal on the 5th July 1928. It appears that no date was fixed for passing the order and the order was passed in the absence of the petitioners. The order, however, was communicated to the petitioners by means of a postcard dated the 7th July 1928 and it is stated by the petitioners in the affidavit before us that the postcard reached them sometime after the 8th July. The application of the petitioners under section 66 clause 2 was posted at Darbhanga on the 4th August 1928 and it was received in the Commissioner's office on the 8th August 1928. At first sight therefore it would appear that the application before the Commissioner was out of time by about 3 days because section 66 clause 2 requires that the application under that section should be made within one month of the passing of an order under section 31 or section 32. Similarly the application to this Court which should have been filed within six months from the receipt of the notice of the order of the Commissioner seems to have been filed a few days later.

Now, it is contended by the petitioners that their application before the Assistant Commissioner was not out of time on two grounds. It is said in the first place that the time is to be computed not from the date of the order but from the date on which the order was communicated to the petitioners. The

second contention is that the petitioners are entitled to claim that the time required for obtaining the copy of the order of the Assistant Commissioner of Income-tax should be excluded in computing the period of limitation. The last ground is also urged to show that the application before this Court was also in time.

As regards the first contention our attention is drawn to the fact that the Assistant Commissioner fixed no time for passing the order and the order was passed in the absence of the petitioners. It is said that it is only just that in these circumstances the period of limitation should be computed not from the date on which the order purports to have been recorded but from the date when the order was communicated to the petitioners, namely, the date on which the postcard was received. It is also pointed out that according to the prevailing practice, the Office of the Income-tax department does not insist on the presence of the party on the date on which the order is to be passed, and as no date is fixed for the passing of the order, the order is always communicated to the party by post. This being so, it is urged that if the period of limitation is not computed from the date of the communication of the order, it may mean great hardship to the party in certain cases because it is possible that the party may not know anything about the order until the period of limitation has expired. Now if the learned Advocate for the petitioners means to point out to us what should be the law, we would say that his argument deserves serious consideration. In the present case, however, our concern is not to lay down what should be the law, but to interpret the law as it stands. In doing so I have to say that I do not find anything in the language of the section to enable me to hold that the expression "passing of the order" should be interpreted as the communication of the order to the party. On the other hand, it is noticeable that while under clause 2 of section 66, time is to run from the passing of the order, it is to be computed under clause 3 from the date on which the assessee is served with notice. Whether this distinction was deliberately made or whether at the time clause 3 was being amended, the language used in clause 2 was not noticed, is difficult to say but it is clear that the plain language of the section does not support the contention of the petitioners. It is true that ordinarily the judgment of a court in order to be properly delivered must be pronounced in court and in fact there is a specific provision to this effect in section 33 and Order XX Rule I of the Civil Procedure Code. There is, however, no such clear provision in the Income-tax Act and I cannot hold without considerably straining the law that the order passed by the Income-tax Commissioner can be ignored for the purpose of limitation, until it has been duly communicated by post to the assessee. All I can say is that what seems to be the hardship of the existing law can be only met by the vigilance of the assesses on the one hand and by the realisation by the Income-tax Department on the other hand that if it does not require the assesses to be present on the day the orders are to be passed, then it is only fair that the orders should be communicated to them as soon as possible after they have been passed.

The second point raised by the learned Advocate for the petitioners appears to me to be much more substantial and they have at least two reported decisions to support them on the point—one of them is a decision of the Rangoon High Court in *Ramanatha Reddiar v. The Commissioner of Income-tax*(1), where it has been held that an assessee who desires to have a reference made to the High Court under section 66 clause 2 of the Income-tax Act on a question of law arising out of an order passed under section 31 or 32 of the Act, is entitled to be furnished with a copy of the reasons for the order and

the time taken by the Office to furnish such copy must be excluded in computing the period of one month allowed to the assessee to apply for the reference.

The other decision was given by the Lahore High Court in the case of *Muhammad Hayat Haji v. The Commissioner of Income-tax, Punjab* (1). In that case the question arose as to whether the days spent in obtaining the copy were or were not to be excluded in computing the period of limitation fixed for presenting an application to the High Court under section 66 clause 3, after the application under section 66 clause 2 had been rejected by the Commissioner of income-tax and it was held that in view of section 29 of the Limitation Act, the period should be excluded.

Now section 29 of the Limitation Act as amended by Act X of 1922 provides as follows:—Where any special or local law prescribes for any suit, appeal or application a period of limitation different from the period prescribed therefor by the first schedule, the provisions of section 3 shall apply as if such period were prescribed therefor in that schedule, and for the purpose of determining any period of limitation prescribed for any suit, appeal or application by any special or local law (a) the provisions contained in section 4; sections 9 to 18 and section 22 shall apply only in so far as and to the extent to which they are not expressly excluded by such special or local law; and, (b) the remaining provisions of this Act shall not apply.

One of the sections referred to here is section 12 of the Limitation Act which provides that in computing the period of limitation prescribed for an appeal, an application for leave to appeal and an application for a review of judgment, the day on which the judgment complained of was pronounced and the time requisite for obtaining a copy of the decree, sentence or order appealed from or sought to be reviewed shall be excluded.

Now, reading the sections together there seems at the first sight to arise a difficulty which was unfortunately not noticed by either party in the course of the argument before us. Section 12 apparently provides that the time for obtaining copies is to be excluded only in case of an appeal, an application for leave to appeal and an application for review of judgment. The question thus arises whether an application under section 66 clause 2 made to the Commissioner of Income-tax or an application under section 66 clause 3 made to this Court will be covered by the provisions of section 12 of the Limitation Act. In my opinion, however, section 29 should be liberally construed and when we turn to that section it appears that it provides for the application of section 12 of the Limitation Act “for the purpose of determining any period of limitation prescribed for any *suit, appeal or application by any special or local law*”. Thus it will not, I think, be straining the law to hold that the main principle laid down in section 12, namely, that the period for obtaining copies shall be excluded in computing the period of limitation in certain cases has been made applicable by section 29 in the case of a suit, appeal or an application under the special law for which a period of limitation has been prescribed and this will cover an application under section 66 (2) and (3) of the Limitation Act. In my judgment, technicalities apart, this will be the only reasonable way of giving effect to the intention of the Legislature. This is the view which seems to have been taken by the Lahore High Court in the case to which I have referred just now and which was a case in which the question of limitation arose in connection with an application made to the High Court under section 66 clause 3. This is also substantially the view of the Rangoon High Court and it finds no little support from the line of reasoning which was adopted in many cases which were decided before the passing of Act X of 1922. In those days

there was nothing in section 29 of the Limitation Act or anywhere else to make the general provisions of the Limitation Act as found in sections 4, 9 to 18 and 22 applicable to any of the special laws or enactments. It was, however, held in a number of cases that these general provisions would apply to a special enactment where that Act is not a complete Code in itself.

To mention only one of the cases in which this view was propounded I may refer to the case of *Dropadi v. Hira Lal* (1) which was decided by a Full Bench of the Allahabad High Court. The following passage which occurs in the judgment of that case may be instructive:—
 “The question is one of considerable difficulty and it must be admitted that at first sight it is straining the words to hold that the application of the general provisions of the Limitation Act to periods of limitation prescribed by other Acts does not ‘affect or alter’ those periods. In one sense it certainly does. But the construction accepted by Strachey, C. J., Benerji, J., and Muthuswami Ayyar, J., seems to us to be correct. Apart from the history of this piece of legislation, we find it difficult to believe that when the legislature introduced, as it has, into several Acts, provisions giving right of appeal and prescribing periods within which the right may be exercised, it intended as a general rule that those provisions should be applied without reference to the general provisions contained in the general Limitation Act. In many, if not most cases, the Code of Civil Procedure is made applicable with the result that an appellant must produce a copy of the order against which he is appealing. It is reasonable to suppose that the Legislature intended to give him time to procure a copy of the order. The general provisions of the Limitation Act are founded mainly upon equitable considerations which apply as much to the period of limitation prescribed by special Acts as to period of limitation prescribed by the Limitation Act itself.”
 I may also quote here the following passage from the judgment of the Rangoon High Court in the case of *Ramanatha Reddiar v. The Commissioner of Income-tax* (2). “It seems to me that when the Legislature allowed thirty days to the subject in which to make an appeal it never intended that the Deputy Commissioner should not communicate his reasons to the assessee at the same time as his bare decision. It is manifestly impossible for any person to make up his mind whether a point of law arises unless he has proper materials to do so before him. The mere statement that his appeal has been allowed or dismissed is not sufficient. It has often been said that revenue statute should be construed in favour of the subject. In my view it is much more important in this connection that any rights of appeal contained in revenue legislation be strictly construed as to their exact meaning as far as they allow specific time in which an effective appeal can be put forward. It can easily be seen that a glut of work in the office of the busy Commissioner may completely deprive an assessee of his right to appeal at all. Such a state of affairs would not be carrying out the intention of the statute and in this case therefore although I think that no conduct of the assessee himself could have enlarged to his advantage the statutory period under the section, neither can any conduct of the executive diminish the full period of time allowed to reflect upon and decide whether action should be taken by way of approach to this Court.”

I am therefore of opinion that although as was laid down in *Ratanchand Khimchand Motichand v. The Commissioner of Income-tax, Bombay* (3) and in *Mothey Ganga Raju v. The Commissioner of Income-tax, Madras* (4), neither the High Court nor the Commissioner has the power to extend the time prescribed by section 66 of the Indian Income-tax Act of 1922, yet on general principles and in view of section 29 of the Limitation Act the assessee is entitled

(1) 84 All. 496.

(3) 2 I.T.C. 225.

(2) 3 I.T.C. 10.

(4) 2 I. T. C. 199.

to have the benefit of the time which was spent in obtaining a copy of the order with which he is dissatisfied. As it is conceded that if such time be excluded the application of the petitioners both before this Court as well as before the Commissioner of Income-tax would be well within time, so in my opinion the preliminary objection raised by the learned Counsel for the Income-tax Department fails so far as it is based on the question of limitation.

There is, however, another point which seems to stand very much in the way of the petitioners. As I have already stated the petitioners were asked by the Income-tax Officer to produce their books of account but they did not produce them. They were given another opportunity to produce any such further evidence as they chose on the 27th July 1928, but they neither appeared before the Income-tax Officer on the date fixed, nor did they produce any evidence on that date. It is said that one of their applications did reach the Income-tax Officer on the 28th and it being stated there that they would rely upon the findings of the Income-tax Officers of Calcutta and Darbhanga, it is contended that this would be sufficient compliance with the notices under section 22 clause 4 and under section 23 clause 2 and no assessment can therefore be made under section 23 clause 4. I find, however, that both the Assistant Commissioner of Income-tax and the Commissioner of Income-tax have held that the petitioners did not comply with the notices under the sections referred to above and that their case came directly under section 23 clause 4.

Now, I have carefully considered the matter and it appears to me that it is not possible for me to say that this view is incorrect. The petitioners were requested by the Income-tax Officer to produce evidence, but they simply turned round and said "we have no evidence to produce and so we want you to decide the case on the materials which are before you". They did not file any affidavit in support of their statement, nor did they make any serious attempt to convince the Income-tax Officer that they had no evidence in their possession. In these circumstances there cannot be any doubt that in substance there was no compliance with the notices under section 22 clause 4 and under section 23 clause 2. There also arises here a technical point in favour of the Crown. Section 23 clause 4 says that an assessment will be made by Income-tax Officer under section 23 (4) if *all* the terms of the notice under the provisions referred to in that section are not complied with. In this case one of the terms of the notice was that the assessee should produce any such evidence as they might choose to produce on the 27th July. No such evidence was however produced by them on that particular date and therefore all the terms of the notice were not complied with. Thus it would perhaps be open to the Income-tax Department to take the view that the case came under section 23 clause 4 although the Income-tax Department neither should, nor I believe, do as a rule take their stand on such a technical ground, in those cases where there is a substantial compliance with its requisition. I am therefore not in a position to say that the decision of the Income-tax Officer that the assessee's case came under section 23 clause 4 under the circumstances of the case is not correct. If so, it is clear that no appeal lay to the Assistant Commissioner of Income-tax from an assessment made under section 23 clause 4 and if no appeal lay in this case, then the provisions of section 66 do not apply and we cannot serve a requisition on the Commissioner of Income-tax to state the case and refer it to the High Court.

I have only to observe here that up to a certain point the petitioners had a good case. It is not clear how the assessment was made on a profit of Rs. 22,000 if the officers of the Department had found, as stated, a profit of Rs. 16,000 in Darbhanga and Monghyr against a loss of Rs. 14,725 in Calcutta. Again, assuming that an appeal lay to the Assistant Commissioner of Income-tax in

this case I do not see how the Assistant Commissioner of Income-tax could throw out the appeal merely because the demand notice was subsequently amended by the Income-tax Officer. A reference to section 30 of the Income-tax Act will show that the appeal lies against the assessment and it is only for the purpose of calculating the period of limitation that the notice of demand is referred to in clause 2 of that section. The order of the Commissioner also is open to criticism on the ground that he has held that the application filed by the petitioner was time barred, although in our opinion it was not. These matters, however, cannot avail the petitioners in the present case, because we can neither go into facts nor proceed under section 66 (3) on account of the legal difficulty that the assessment being made under section 23 (4) no appeal lay from that assessment. It is clear that the petitioners have considerably weakened their case by not producing their books of account and by setting up the plea which has been rejected everywhere that their books which were in existence in the years 1923 and 1924 have since been destroyed by whiteants. In my opinion the application ought to be dismissed, but under the circumstances of the case there will be no order as to costs.

CHATTERJI, J.:—I agree.

(321) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Niamatullah.

(25th July, 1929.)

Ganga Sagar	.. .. .	Petitioner*
v.		
Emperor	.. .. .

Indian Income-tax Act (XI of 1922), Secs. 52, 22 (2) and (3)—Return containing false statement—Offence when committed—Subsequent filing of revised true return, effect of—Scope of Sec. 52.

An offence under Sec. 52 of the Income-tax Act is committed on the day the return made under Sec. 22 (2) is verified by an assessee and a revised return of his true income filed under Sec. 23 (3) will not condone the offence, though it might go in its mitigation.

A letter sent by an assessee accompanied by a statement of his income together with the printed return form in blank would amount to the making of a return within the meaning of Sec. 22 of the Income-tax Act.

The provisions of Sec. 52 of the Income-tax Act for compounding an offence thereunder are not intended to confer on the Income-tax authorities power to obtain as much money as possible by holding out a threat of prosecution.

Criminal Revision Petition No. 326 of 1929 preferred against the order of the Sessions Judge of Bulandshahr dated the 5th March, 1929.

*Sir Tej Bahadur Sapru, Nehal Chand and P. N. Sapru, for the Petitioner.
U. S. Bajpai, for the Crown.*

* A. I. R. (1929) All. 919.

JUDGMENT

MUKERJI, J.:—This is an application to revise the order of the District Magistrate convicting the applicant under section 177, Penal Code read with section 52, Income-tax Act, and sentencing him to pay a fine of Rs. 1,000 and the order of the Sessions Judge, in appeal, confirming the said conviction and sentence. On behalf of the Crown a revision has been filed, being revision No 311 of 1929, praying that the sentence passed on Rai Bahadur Seth Ganga Sagar may be enhanced on the ground that it is inadequate. As the result of the revision filed on behalf of the Crown, the question whether the applicant's conviction is good on facts, has been re-opened. We have heard the learned Counsel for the parties at length. The facts which led to the conviction of Mr. Ganga Sagar briefly are these.

Mr. Ganga Sagar is a wealthy trader of Khurja in the District of Bulandshahr. He holds a large amount of shares in different companies including many jute mills in Bengal which pay very handsome dividends. He was to be assessed with income-tax and the Income-tax Officer Mr. Samiullah, served him with a notice for making a return of the income earned by him in the year 1926—1927, so that on the basis of that income the tax payable by him for the year 1927-28 might be assessed. The notice was issued on 2nd April 1927, and by it the return was to be filed on 15th May 1927. The applicant, Mr. Ganga Sagar, took time for preparing the return and, ultimately, on 20th July 1927, appeared personally with his books before Mr. Samiullah. It is important to note that 25th July 1927 had not been fixed for the appearance of Mr. Ganga Sagar, nor had the date been fixed for him to produce his account books. His only duty was to file a statement of his income. Mr. Samiullah was requested by Mr. Ganga Sagar to examine his (latter's) account books and to satisfy himself as to the income of the proposed assessee. Mr. Samiullah ought to have plainly told the applicant that it was no part of his (Mr. Samiullah's) duty to examine the account books for the benefit of Mr. Ganga Sagar and it was for Mr. Ganga Sagar to find out from his own books, what his income, under the several heads, was and to make a return. Mr. Samiullah, however, was persuaded to accede to Mr. Ganga Sagar's request and he noted down on two pieces of paper what was the income of Mr. Ganga Sagar, according to his books. After the several items of income had been added up, Mr. Ganga Sagar entered those figures in the form provided for making a return by an assessee, and he signed it. This return is Ex. P, and the note made by Mr. Samiullah is Ex. O. Mr. Samiullah, after the return had been made, recollected that he had some information conveyed to him by the Income-tax Officer of "Companies District" that Mr. Ganga Sagar had received a dividend of Rs. 6,000 on account of his shares in Sura Jute Mills, Ltd. Mr. Samiullah asked Mr. Ganga Sagar how it was that this dividend did not find place in his books. Mr. Ganga Sagar replied, according to Mr. Samiullah, that the date of payment as recorded in the letter of the Income-tax Officer of Companies District (Ex. N.), was merely the date of the declaration of the dividend. The suggestion conveyed by this reply was that the actual dividend had not yet been received by Mr. Ganga Sagar. This set Mr. Samiullah thinking and he made certain further enquiries as to Mr. Ganga Sagar's income from dividends. The enquiries took the shape of a letter addressed to the Calcutta Income-tax Office. Mr. Samiullah also got certain information from the companies intimating what dividends had been paid to Mr. Ganga Sagar.

The letter Ex. V and the enclosures Ex. VI to Ex. V-5 show that Mr. Ganga Sagar had received dividends to the amount of about Rs. 70,000 over and

above the dividends that had been declared in the return made on 25th July 1927. Before receiving Ex. V Mr. Samiullah had already issued notice to Mr. Ganga Sagar to produce his account books for the Sambat year 1981 to 1982. I may mention here that the Hindu year for which Mr. Ganga Sagar was expected to make a return was 1982 to 1983, Dewali to Dewali, corresponding to 17th October 1925 to 5th October 1926. On receipt of Ex. V and its enclosures, he issued another notice, on 19th October 1927, calling on Mr. Ganga Sagar to make a return of his income for the previous year, on the ground that a portion of the income of that year had "escaped" assessment. Evidently the Income-tax Officer thought that Mr. Ganga Sagar had a much larger income than for which he had made a return and that he had not fully disclosed his income either for the year 1982 to 1983 or for the previous year. Mr. Ganga Sagar admits in his statement before the Court that he received the notice by the end of October 1927. Then he consulted some friends and, as the result of what he was told, he sent a letter from Calcutta to the Income-tax Officer (Mr. Samiullah) at Bulandshahr stating that he had made a mistake in the figures supplied by him on 25th July 1927. This letter is Ex. W and was received in the office of the Income-tax Officer on 7th November 1927. Attached to this letter was a statement of the income in Hindi. This has been marked as Ex. W-1. Along with this letter and the enclosure, Mr. Ganga Sagar sent one of the printed forms in Hindi, in which an assessee is required to make a statement of his income. He said in the letter Ex. W in Hindi (while the letter itself is in English) that he did not know how to fill up the form. The suggestion was that the Income-tax Officer might enter the figures contained in Ex W-1 into the blank form W-2 and substitute the fresh return in place of the return made on 25th July 1927. The letter Ex. W runs as follows:—"I find that during your inspection of my *bahikhata* on 25th July 1927, you omitted to look into certain entries. As you yourself had looked into it I believed that you should have examined the whole of it. Just then in your presence in a hurry I prepared the statement and gave it over to you. Since then I had been busy in other works. Now on Dewali when I went into the accounts to carry over into the *bahikhata* I found that mistakes had crept in the examination of accounts. The statement that I prepared in a hurry in your presence and gave to you was not quite accurate. I herewith send another correct statement. The former is not correct. This is correct according to accounts. Please cancel the former statement and put this revised one on file." It is common ground that Ex. W-1 submitted with this letter Ex. W contains substantially a correct statement of the applicant's income.

The applicant was assessed on an income of Rs. 4,73,045 with a tax of Rs. 2,761 and odd and super tax of rupees 75,951 and odd. He was also assessed on account of the previous year (1926-27) on the ground that a considerable portion of his income has escaped assessment. The basis of this assessment made under section 34 (escaped items) was Rs. 5,00,000.

Negotiations were then started with Mr. Ganga Sagar calling on him to pay a sum of Rs. 7,00,000 on pain of being prosecuted for having made a false return on 25th July 1927. Mr. Ganga Sagar did not agree to pay this large sum and the Income-tax authorities came down to the sum of Rs. 3,00,000. Even this sum Mr. Ganga Sagar refused to pay and then his prosecution was ordered, not only under section 52, Income-tax Act, read with section 177, Indian Penal Code, but also under section 193 (perjury) and section 465 (forgery) of the same Code.

As the result of a trial before the District Magistrate of Bulandshahr, Mr. Ganga Sagar was acquitted of the offences under sections 193 and 465 Indian

Penal Code and was convicted of the offence under section 177 (read with section 52, Income-tax Act), Indian Penal Code and was sentenced as already stated.

As I have already stated, the whole evidence has been thoroughly thrashed out and all possible arguments have been put forward on either side before us. Having considered the evidence I am fully satisfied that Mr. Ganga Sagar when he filed his return on 25th July 1927 either knew or believed that it was false or at least did not believe that it was true. If that it is so, he has been rightly convicted. I shall examine the evidence very briefly (an extensive survey of the evidence is not called for). But before I do so it is necessary to examine the contention of Sir Tej Bahadur Sapru on behalf of Mr. Ganga Sagar that, under the law, Mr. Ganga Sagar was not at all liable to be prosecuted inasmuch as he filed a fresh return which was received in the Income-tax Officer's office on 7th November 1927 and which was substantially correct. For the Crown it is urged that this supposed return was no return at all, for the form provided for preparing a return was not filled in nor signed. I am not prepared to attach much importance to this pure technicality. I take it that the letter Ex W and its enclosure Ex W-1 and the blank form sent by the applicant did substantially amount to the making up of a return. Because Mr. Ganga Sagar filed a correct return on 7th November 1927 (this is the date of the receipt), is he not liable to be prosecuted under section 52, Income-tax Act?

Section 52 reads as follows, so far as it is relevant at the present moment. "If a person makes a statement in a verification mentioned in..... section 22,.....which is false, and which he either knows or believes to be false, or does not believe to be true, he shall be deemed to have committed the offence described under section 177 Indian Penal Code." On a plain reading of this provision of law an offence is committed on the day a return made under section 22 is verified by a party. It follows that on 25th July 1927 Mr. Ganga Sagar did commit an offence under section 177, I.P.C., if he made a statement which was false and which he either knew or believed to be false or did not believe to be true. This return was made by Mr. Ganga Sagar under section 22 clause (2), Income-tax Act. In the same section, clause (3) says that where a person has not furnished a return or having furnished a return "discovers any omission or wrong statement therein" he may furnish a return or a revised return as the case may be, at any time before the assessment is made and any return so made shall be deemed to be a return made in due time under this section. Sir Tej Bahadur argued that when Mr. Ganga Sagar furnished a revised return which was received on 7th November 1927 the earlier return, Ex. V was "washed out" and it could not be used even for the purpose of prosecution.

There is nothing in clause (3) section 22 which says that any offence committed with respect to a return made under clause (2) section 22 must be condoned if the revised return be true. All that clause (3) provides is that this return would be treated as a return made in due time, provided it is made before an assessment has been made. In my opinion clause (3) does not go in any way beyond this. The result is that if, on facts, Mr. Ganga Sagar be found guilty with respect to the return Ex. V he must be convicted. It may be that the fact that Mr. Ganga Sagar made a revised and correct return may go in mitigation of the offence but the offence once committed is there and a conviction is bound to follow unless it is compounded under section 53 clause (2), Income-tax Act.

Now as to facts. Mr. Ganga Sagar knew that his income from the dividends received from various companies was Rs. 3,47,000. In the return that he made in the presence of Mr. Samiullah (Ex P.), he put down the income at

Rs. 62,000 and odd. His explanation is two-fold. First he says that he put down his books before Mr. Samiullah, Mr. Samiullah examined the accounts, noted the income and then Mr. Ganga Sagar put down the figures found by Mr. Samiullah in Ex. P. This is no doubt true, but it is equally true that Mr. Samiullah was not fully cognizant of all the entries in the applicant's books, and the applicant knew that this was the case. What the applicant has done as regards the entry of the dividends in his books is this. At p. 37 of his account book he has entered under the heading "income from shares" certain amounts received from certain companies totalling to Rs. 62,000 and odd. At p. 39 he put down certain figures with reference to pages of "*naqal bahi*". The heading of this page is "account of profit and loss relating to shares." If this p. 39 be read with the *naqal bahi*, the entries would show that large sums of money, amounting to nearly three lakhs of rupees, were received by Mr. Ganga Sagar from companies other than those mentioned at p. 37, and the amounts so received were entered in the book by him in a particular manner. He purchased certain new shares at a premium. What Mr. Ganga Sagar did was to debit himself with the amounts he paid over and above the face values of the shares, on the ground that the price paid by him over and above the face value represented his loss in the transactions of the purchase of the new shares.

It is clear from what took place on 25th July 1927 before Mr. Samiullah that Mr. Ganga Sagar did not disclose to Mr. Samiullah the fact that he had received other dividends also (dividends other than those shown at p. 37) and that he had recorded in his books those dividends in a particular manner. When Mr. Samiullah asked where the entry as to the dividend paid by Sura Jute Mill was entered, Mr. Ganga Sagar gave an evasive reply. He did not disclose the fact that this income (which amounted to Rs. 18,000) had been used by him in purchasing further shares. It has been contended on behalf of Mr. Ganga Sagar that the latter, most foolishly, but honestly, believed that if he employed a part of his income in purchasing shares at prices which went beyond the face values he would be entitled to treat the excess amount so paid above the face value as his loss and he would be entitled to deduct the same from his total income and to show the balance alone as his real income. On the evidence given by Mr. Chatura Dutt Joshi, a Deputy Collector, there can be no doubt that Mr. Ganga Sagar did think that he might escape payment of heavy income-tax and still heavier super-tax if he could show that he had suffered a loss in his dealing with shares. Mr. Chatura Dutt Joshi, whose evidence is beyond suspicion and has never been challenged, stated that the applicant met him at Cawnpore and spoke to him about his investments and asked him if he was not justified in debiting himself as with a loss, with the amounts paid by him in excess of the face values of the shares. Mr. Chatura Dutt Joshi plainly told him that he could not do so and Mr. Ganga Sagar argued that the money so spent was really his "loss". This happened either at the end of October or early in November 1927. Soon after that Mr. Ganga Sagar sent him the letter and statement of accounts already mentioned (Exs. W and W-1).

On the basis of the evidence of Mr. Chatura Dutt Joshi, Sir Tej Bahadur has argued and with great vehemence that the applicant was under the honest but extremely foolish impression that he was entitled to deduct the money invested as described from his total income and to show the balance as his real income. I am prepared to concede and it must indeed be conceded that a man who is liable to pay a tax is entitled to take shelter under all devices which he may adopt within the law, to avoid payment of the tax. Indeed, the whole scheme of the Indian Income-tax Act contemplates that people liable to be assessed with the income-tax were likely to shirk making true disclosures and if they did go wrong they were to be treated with more or less leniency. But it

does not follow that a person who has made a return can legitimately suppress matters within his knowledge.

Mr. Ganga Sagar did not disclose to Mr. Samiullah the fact that he had received dividends from companies other than those mentioned at p. 37 of the *Khata Bahi*, and that he had invested them in such a way as to entail him a supposed loss. If Mr. Ganga Sagar had done that, he would have disclosed the whole truth and, then, the question would have been for decision by the Income-tax Officer and his superior officers and perhaps ultimately by the High Court, whether Mr. Ganga Sagar was entitled to the deduction he claimed. There can be no doubt that Mr. Ganga Sagar did not want to commit himself definitely by making a return on his own responsibility. That is why he took all his books to the Income-tax Officer and laid them before that gentleman. But it was not to be expected that Mr. Samiullah would be able to find out what were the entries at p. 39 of the *khata* book and whether they, if read with the entries in the *naqal bahi* showed that Mr. Ganga Sagar had received dividends other than those noted by Mr. Samiullah himself in Ex. O. Then it is conceivable, and indeed I am prepared to accept the statement of Mr. Ganga Sagar, that he thought that he would be able to escape payment of tax on sums invested by him in the manner already described. But the question is, did he really believe when he said that his total income from dividends was Rs. 62,000, that he was making a correct statement? Mr. Ganga Sagar was perhaps trying to hoodwink himself and was trying to quiet his conscience, by the method adopted by him for avoiding the payment of the income-tax. But in spite of that, it is difficult to believe that he believed it to be true that the statement Ex. P. contained correct figures, against the head "dividends". I hold that the conviction is right.

Now I come to the question of sentence. I note that not a single ground for revision has been taken on behalf of Mr. Ganga Sagar that the sentence passed against him is excessive. Nor has the Court been addressed on the ground of severity of the sentence. The reason is clear. Mr. Ganga Sagar is a very wealthy man and it is the conviction that he minds and not the amount of the fine that has been imposed on him. The learned District Magistrate has imposed the maximum fine that is provided by law under section 177, Indian Penal Code, and has remarked that the case did not call for any sentence of imprisonment. He said: "Coming to the question of sentence I realize that even the maximum sentence of fine which I can inflict will be no real punishment for a rich man like the accused. At the same time the moral stigma attaching to the accused for conviction is sufficient, in my opinion, to make a sentence of imprisonment unnecessary."

Although I agree with the latter portion of his remark, in my opinion the learned Magistrate was entirely wrong in the principle he adopted in awarding the sentence. The maximum sentence whether of fine or of imprisonment, provided for by law, represents the sentence to be inflicted in extreme cases. Because a man may easily pay a fine is no ground for ordering him to pay the maximum fine fixed by law, if the nature of the offence committed by him is not of the most serious character, having regard to the description of the offence itself. Take, for example, a conviction under the Motor Vehicles Act. Almost all the owners of private motor cars are well-to-do people. If a minor motor rule is infringed, on the principle adopted by the learned Magistrate, the maximum fine provided by the rule must be inflicted, because the owner of the motor can easily pay that amount. No doubt, the Court must look to the means of the accused person, his respectability, his standard of living and all similar matters in inflicting a sentence. In technical cases, a few rupees would be enough even though the convicted

person be a rich man. In the case of a very poor man, a small fine may really be heavier to him than a short term of imprisonment. But, from the fact that the accused person is a rich man, it does not follow that he must pay the full penalty provided by the law, irrespective of whether the nature of the offence committed by him demands it or not.

The foregoing remarks are relevant to the application made on behalf of the Crown for enhancement of sentence. It has been urged by the learned Government Advocate that a sentence of Rs. 1,000 is nothing to Mr. Ganga Sagar and the Courts below should have sent him to jail, and that we should do the same now. In my opinion the application for enhancement is entirely ill advised in this case. If I had been trying the case as a Magistrate, I would never have sentenced Mr. Ganga Sagar to a fine exceeding Rs. 250. There can be no doubt that he tried to escape payment of taxes. An anxiety to escape the payment of a tax amounting to Rs. 78,000 out of a total income of Rs. 4,00,000 is almost natural. His anxiety to escape payment of this tax led him to invent the idea of debiting himself with a supposed loss in the manner already described above. I have already pointed out that the talk with Mr. Joshi establishes that Mr. Ganga Sagar was prepared to defend his action. Mr. Ganga Sagar did after all send a revised statement of his income which was true. No doubt he did this after he had been called upon to produce his account books of the previous year and to make a return of his income of the previous year. But when he made the revised return, he did not know what materials the Income-tax Officer had in his possession for proving his income. Indeed, the materials showed only an additional income of Rs. 75,000 and odd and not nearly Rs. 3,00,000 declared on 7th November 1927. The law does contemplate making of revised returns and does contemplate cases, where incomes which ought to have been taxed, have escaped taxation. Section 28, Income-tax Act, provides for penalty for concealment of income. It says: "If the Income-tax Officer.....is satisfied that an assessee has concealed the particulars of his income or had deliberately furnished inaccurate particulars of such income and has thereby returned it below the real amount, he may direct that the assessee in addition to the income-tax payable by him, pay by way of penalty a sum not exceeding the amount of income-tax which would have been evaded if the income, so returned by the assessee, had been accepted as the correct income".

The legislature knew that it would be hard for a person to tell the truth when the telling of the truth meant a payment of money and a heavy sum of money in some cases. Few people would be expected to realise the fact that taxation is necessary for the carrying on of the Government and, therefore, they should pay the tax ungrudgingly and honestly. People always grumble at taxation, however necessary and the Income-tax Act did recognise this fact when it made the offence under section 52 a compoundable one, although the offence under section 177 Indian Penal Code itself is not compoundable.

Then again, Mr. Ganga Sagar put all his books before the Income-tax Officer. No doubt, in doing this, he wanted to act "within the law". He thought that he would not take the risk of making a false return and would let the Income-tax authorities discover, if they can, from his books, what his total income was. All this would go to show that Mr. Ganga Sagar was struggling between his anxiety to save his money and fear of committing anything which was unlawful.

For reasons best known to them, the Income-tax authorities did not take action under section 28 of the Act. If they had taken action under that Act they would have, probably, been in a position to realise nearly Rs. 70,000 from

Mr. Ganga Sagar. They under the law could not realise more than that, even if Mr. Ganga Sagar had managed to escape payment of lawful taxes for several years. Knowing that, the Income-tax authorities tried to realise, I had almost used the word "extort", Rs. 7,00,000 from Mr. Ganga Sagar. Ultimately they came down to Rs. 3,00,000: *Vide*, the statement of Mr. Bhawan, Income-tax Officer. They were prepared to compound the offence, if Mr. Ganga Sagar paid Rs. 3,00,000. But what did the sum of Rs. 3,00,000 represent? The Government Advocate has told us that Rs. 3,00,000 were really only a small portion of the taxes Mr. Ganga Sagar should have paid in the course of several previous years. We have no evidence on the point and, even if this were true, the law did not provide for recovery of taxes on "escaped income" for more than one year; see section 34. The Income-tax authorities were, therefore, trying to realize by the threat of prosecution, what they could not realize under the law. This is a hardly desirable conduct in officers of the Government who are really servants of the State and, therefore, of the people. Then, I am rather surprised to find that when the negotiations for compounding the offence fell through, Mr. Ganga Sagar was charged not only with an offence under section 177 Indian Penal Code, but also with offences under sections 193 and 465 Indian Penal Code. Neither the offence under section 193 nor the offence under section 465 Indian Penal Code, is compoundable. If the Income-tax authorities believed that Mr. Ganga Sagar had committed offences under those two sections of the Indian Penal Code, they had no right to drop the prosecution under these sections on receipt of money. The talk of compromise could only have related to the offence under section 177, Indian Penal Code read with section 52, Income-tax Act. In that case, on the failure of the compromise, no prosecution under sections 193 and 465 should have been ordered. The officers of the Crown, therefore, on whose behalf the learned Government Advocate is now pressing for a sentence of imprisonment have hardly been fair in their dealings with Mr. Ganga Sagar, and the prayer for a sentence of imprisonment comes but with ill grace from their mouth.

In the result I would dismiss the application in revision made by Mr. Ganga Sagar as also the application for revision made on behalf of the Crown.

NIAMATULLAH, J.:—The facts of the case have been stated at length by my learned colleague, with whom I entirely agree in the conclusions arrived at by him. It is no longer in dispute that the applicant showed only part of his income in the return which he made on 25th July 1927. A sum of Rs. 2,47,795 had been received by him as dividend on his shares in a number of jute mill concerns, which he invested in the purchase of new shares of the face value of Rs. 62,000 odd. The difference between the face value and the actual price paid therefor (which came to several times the face value) represented the price he had to pay above par. He showed Rs. 62,000 odd as the amount of dividends received by him, as, according to the account which he produced before the Income-tax Officer, Bulandshahr, on 25th July 1927, that amount alone represented his income under that head. The remaining amount (i.e., the difference between the face value of the shares purchased and the actual price paid) was entered in the account books as a loss, in a khata headed as "profit and loss of shares". It was not till 7th November 1927, or thereabout, that he attempted to rectify the error by his letter, Ex. W, and the accompanying details given in Ex. W-1.

The contention put forward on his behalf and strenuously urged by Sir Tej Bahadur Sapru, is that he showed Rs. 62,000 odd, on 25th July 1927, as the net amount of dividends received by him in consequence of a mistaken notion of his that anything paid for shares over and above the face value of the

shares purchased should be considered to be his loss. I am unable to accept this contention. No one who has even an elementary knowledge of business principles, much less a man of the position and antecedents of the applicant, can possibly think that any part of the money invested in the purchases of the shares of the face value below the price paid can be put down as a loss. The mere fact that he considered it worth his while to pay several times more than the face value of the shares is a proof positive of the value which he placed on such shares. It is obvious that, if he had regarded the investment as a losing bargain, he would have refrained from making the investment.

The circumstances under which the return was made on 25th July 1927 leave no doubt in my mind that the applicant did not believe the statement contained therein to be true. He had received a notice early in April to submit a return by 15th May 1927, when an extension of time was granted till 15th June 1927. Another extension of one month was obtained, but no return was made. On 25th July 1927, the applicant appeared in person before the Income-tax Officer with his account books. The Income-tax Officer examined the khata in which receipt of dividends had been shown, and within a comparatively short time prepared Ex. O, in which various receipts of dividends were noted and totalled as Rs. 62,000 odd. The applicant, who had refrained for over two months from making his return, found his opportunity to take the Income-tax Officer at his own word, and prepared a statement there and then, entering the amount noted by the Income-tax Officer as his dividend. If he had believed that the amount shown as his dividend in the khata, which the Income-tax Officer accepted, was the correct amount, he would have himself prepared a return long before 25th July 1927 instead of obtaining extensions, as he did. It seems to me that he knew the state of his account, and was not prepared to take the responsibility of submitting a return showing Rs. 62,000 odd as the only dividends received by him, the rest of it being loss according to another khata of his account. When he found that the Income-tax Officer himself arrived, on examination of his account, at the figure 62,000 odd as his receipts from dividends, he considered it quite safe to prepare a statement there and then according to the figures noted down by the Income-tax Officer himself. That he had previously prepared his account to support the plea that the major part of the dividends represented the price paid by him over and above the face value of the shares purchased and, therefore, a loss to that extent, is not open to question; but he realised that the plea was not likely to be accepted and did not, therefore, prepare his statement before he found the Income-tax Officer to have arrived at the figure 62,000 odd on a cursory examination of his accounts. It is significant that he did not mention to the Income-tax Officer on 25th July 1927, that his account in respect of the dividends was made up in the manner in which it had been prepared. On the contrary, it is clear that he concealed from the Income-tax Officer entries of part of receipts of dividends in the profit and loss khata of his account. On being questioned by the Income-tax Officer regarding the receipt of certain dividends referred to in the letter received by the latter from the Income-tax Officer of companies, he gave evasive replies, suggesting that the letter referred to receipts of dividend which had not been actually received till then, though as a matter of fact, part of it at any rate was entered in the profit and loss khata.

Reliance has been placed upon the evidence of Mr. Chatur Dutt Joshi in support of the plea of good faith on the part of the applicant. As I read his evidence it does not support the case which is sought to be built on it. He says: "I came to Cawnpore from Azamgarh about 30th October, 1927, to give evidence in a case before the Sessions. I went back from Cawnpore

probably on 1st November, or 2nd November. In Cawnpore I met Seth Ganga Sagar at the house of Pandit Rameshar Dayal, Deputy Collector. He asked me a question about his income-tax. The question was whether he would be liable to pay tax on the money which he had spent out of his income in buying shares above their face value. I told him he would be so liable and he said it really represented his loss. I said that might be so, but no one would accept that view and it would be taxed. He was going to Calcutta. I told him he could consult people in Calcutta and send in his return accordingly."

This statement of Mr. Chatur Dutt Joshi itself shows that the applicant had misgivings in his mind. He had adopted a queer system of account, which was nothing short of a device to obtain exemption from payment of income-tax in part. He consulted Mr. Joshi to ascertain if there was any chance of the device being successful and the answer was what he probably expected. The incident does not show that he believed on 25th July 1927 that his income from dividends was no more than Rs. 62,000 odd. He had been previously examined by the Assistant Commissioner of Income-tax, on 2nd September 1927, regarding certain dividends not included in the Rs. 62,000 odd entered in his statement of 25th July 1927. He had also received a notice, dated 19th October 1927 requiring him to submit a return of income which had escaped assessment. He must have been aware of the practice of the Income-tax Officers of companies receiving regular information from the companies regarding payment of dividends to the recipients, and communicating the same to the Income-tax Officers of various districts. It was not unnatural, under these circumstances, for the applicant to have become nervous by 1st November 1927 when he met Mr. Chatur Dutt Joshi, to whom he mentioned his peculiar views in the matter of investment of money in shares purchased above par, and subsequently wrote the letter Ex. W-1, which disclosed the actual amount of dividends received by him, namely Rs. 3,42,795.

It has been urged on behalf of the applicant that Exs. W and W-1 should be regarded as a revised return within the meaning of section 22 (3), Income-tax Act, which permits a *locus penitentiae* to the assessee. If an action, such as this, of the applicant, can be properly styled *locus penitentiae* and a revised return under section 22 (3) it may have the effect of relieving him of the consequences contemplated by section 23(4), i.e., liability to be assessed according to the best judgment of the Income-tax Officer, from which no appeal is allowed, but cannot condone the offence, if any, under section 177 Indian Penal Code read with section 52 Income-tax Act, previously committed. If once it is established that the applicant made a statement in a verification mentioned in section 22 which was false and which he either knew or believed to be false or did not believe to be true, the offence was complete at the time when the statement was made. The essence of an offence under those sections lies in the verification of an untrue statement, and provided the statement was deliberately false or not believed to be true, subsequent rectification cannot make it any the less an offence, though it may be considered as an extenuating circumstance in awarding sentence. I have found above that the applicant did not believe on 25th July 1927 that his income from dividends during the period in question was believed by him to be what he showed in the return of that date. It follows that he committed on that date an offence under section 177, Indian Penal Code read with section 52, Income-tax Act. For the reasons stated above, I agree with my learned colleague in dismissing the revision, which I hereby do.

As regards the sentence, I accept the reasons given by the learned District Magistrate for awarding the maximum sentence of fine without adding to it any sentence of imprisonment. As has been pointed out by my learned colleague, it is not always possible, nor desirable, that a deterrent sentence

should be aimed at. The circumstances of each case have to be considered in awarding sentence, and I am not prepared to say that the course adopted by the learned Magistrate was faulty. If a sentence of fine only is to be regarded as lenient, any sentence of imprisonment, simple or rigorous, is too severe for a man in the position of the accused. It is to be noted that the Income-tax authorities could have, if they had so chosen, imposed a heavy penalty equal to one year's tax under section 28, Income-tax Act. They did not avail of the provisions of that section, because, as it appears to me, an attempt was made to recover from the applicant a very much larger sum for compounding the offence which he was alleged to have committed. It is in evidence that a sum of seven lakhs was originally demanded from him for allowing the case to be compounded. The demand was reduced to three lakhs later on. The applicant did not accede to the demand and was prosecuted not only for an offence under section 177, Indian Penal Code read with section 52, Income-tax Act, but also for serious offences like perjury and forgery, which could not be substantiated. The Act empowers the Income-tax authorities to compound offences on receipt of money; but it was never the intention of the legislature that the power conferred by it should be used to obtain as much money as possible by holding out a threat of prosecution. It seems to me that action under section 28, Income-tax Act, was not taken because the applicant refused to pay the large sum of money demanded from him for compounding the offence which he was alleged to have committed, and the anxiety to have him sentenced to a term of imprisonment for his contumacious behaviour was vindictive.

For the reasons stated above, I agree with my learned colleague in refusing to enhance the sentence awarded by the District Magistrate.

(322) IN THE HIGH COURT OF JUDICATURE AT FORT WILLIAM
IN BENGAL

*Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose
and Mr. Justice Buckland.*

(2nd August, 1929.)

Lachhiram Basantalal Basantlal Nathani

... Assessessees*

v.

The Commissioner of Income-tax, Bengal.

.. Referring Officer

Indian Income-tax Act (XI of 1922), Sec. 5 (4)—Commissioner appointing officer to deal with individual cases—Jurisdiction.

Sec. 5(4) of the Income-tax Act does not empower the Commissioner of Income-tax, Bengal, to appoint an Income-tax Officer to perform all the functions of the Income-tax Officer in respect of those persons in Calcutta whose cases may be made over to him by the Commissioner from time to time.

Case stated under Sec. 66(1) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

In accordance with the provisions of section 66(1) of the Income-tax Act, I have the honour to refer the following case for the decision of the Hon'ble High Court.

2. The following are the facts of this case.—Messrs. Lachhiram Basantalal Basantalal Nathani, hereafter called the assesseees, a Hindu undivided family having their offices in Calcutta, are merchants carrying on money lending and share businesses. They also own house property and receive dividends. Their accounting year is Ramnavami which usually ends in April. On the 15th December 1927 the Special Income-tax Officer issued a notice under section 22 (2) of the Act calling for a return of their income during the previous year, viz., 1983 (Ramanavami) by the 22nd January 1928. On the 23rd January 1928 a petition was filed stating that owing to the prolonged illness of Babu Basantalal Nathani, the proprietor of the firm, to which he ultimately succumbed on the 5th December 1928 the business was at a standstill, and no proper books of account were kept, and so they were unable to "return an accurate income". On the 31st January 1928, the Income-tax Officer issued a notice under section 22(4) calling for accounts of the accounting year and three previous years and other documents specified therein for the 16th February 1928. On this day the assesseees applied for a fortnight's time for their production. The Income-tax Officer allowed time and fixed the 28th February 1928 for compliance with the notice under section 22(4). On the 28th February 1928 the return was filed. Thereupon, on the 1st March 1928, the Income-tax Officer issued a combined notice under sections 23(2) and 22(4) asking the assesseees to produce any evidence upon which they might rely in support of the return and complete sets of accounts of the year 1981, 1982 and 1983 (Ramanavami), inclusive of the accounts of all branches and other documents specified in the notice, on the 14th March 1928. On the 14th March 1928, the case was adjourned to the 17th March 1928 and again to the 21st March 1928, at the request of the assesseees' pleader. On the latter date a statement regarding dividends received in the previous year was filed but no other evidence or accounts were produced. On this day a fresh combined notice under sections 23(2) and 22(4) was issued calling for evidence in support of the return and accounts for 1981, 1982, 1983 and 1984 (Ramanavami) and other documents mentioned therein for the 29th March 1928. On the 29th March 1928, the Income-tax Officer adjourned the case to the 30th March 1928, at the request of the pleader, who signed the order sheet in token of his having seen the order. On the 30th March 1928, the petitioners or their representatives did not appear, nor were any accounts or evidence produced, and the assessment was made on that day under section 23(4) for non-compliance with the notice under sections 23(2) and 22(4).

On the 21st April 1928, the assesseees presented a petition under section 27 stating that they were prevented by certain unavoidable circumstances from complying with the Income-tax Officer's requisitions. The Income-tax Officer however rejected the petition holding that sufficient time had been granted.

Against the Income-tax Officer's order under section 27 refusing to re-open the assessment the assesseees filed an appeal before the Assistant Commissioner of Income-tax, in which a fresh plea which was not raised at the time of assessment or in the petition under section 27, was taken that the Special Income-tax Officer had no jurisdiction to assess them. The Assistant Commissioner upheld the order of the Income-tax Officer under section 27. As regards the question of jurisdiction he held that such a question could not arise in appeal, probably because he thought that in an appeal against the Income-tax Officer's order under

section 27 he was, in the circumstances of the case, only competent to consider whether the assessee was prevented by sufficient cause from complying with the Income-tax Officer's requisitions, though he did not say this.

The assessee has now petitioned me to revise the Assistant Commissioner's order under section 33, or in the alternative to make a reference on the following two questions of law:—(1) Whether the Special Income-tax Officer had any jurisdiction over your petitioners' case within the meaning of sub-sections 4 or 5 of section 5 of the Income-tax Act? (2) Whether the Assistant Commissioner was legally justified in taking the report of the Income-tax Officer as the basis of his order while that report for the first time introduced a new fact which the petitioners had no opportunity or occasion to challenge or controvert at the hearing? I have declined to interfere in revision.

As regards the question of law which I am asked to refer to the Hon'ble High Court I am of opinion that question 1 does not arise out of the Assistant Commissioner's order on appeal, and I cannot therefore refer this question under section 66(2).

Question 2. The facts regarding this question are that the Special Income-tax Officer reported to the Assistant Commissioner of Income-tax in connection with the appeal proceedings that on the 29th March 1928, the assessee's pleader appeared before him with a Gomastha and asked for three days' time on the ground that he had to leave Calcutta for a few days. The Special Income-tax Officer did not grant the time in as much as enough time had then been granted and the financial year was drawing to a close. The date of hearing was then fixed for 30th March 1928, and the assessee's pleader told him that in that case he would not be present personally, and that the books would be produced by the Gomastha. The fact of a Gomastha having accompanied the pleader was not recorded in the order sheet, but the Special Income-tax Officer reported that he distinctly remembered his having done so. The Assistant Commissioner stated in his order on appeal that he accepted the report of the Special Income-tax Officer. So the assessee contends that the Assistant Commissioner introduced a new fact in his order in accepting the Income-tax Officer's report. I may point out in this connection that it is immaterial whether the assessee's Gomastha was present or not when the Income-tax Officer passed his order of the 29th March 1928. It was sufficient that the assessee's duly accredited pleader was present, and signed the order sheet in acknowledgment of his having seen the order. As the question does not affect the merits of the case I am not inclined to refer it.

In the circumstances I cannot refer either of the questions under section 66(2) of the Act.

As question 1 is, however, of considerable importance I am inclined to refer it under section 66(1). The assessee's argument in connection with this question is that the Special Income-tax Officer had no jurisdiction to assess them, as he was not the regular Income-tax Officer of the district in which they carry on their business, and so long as the regular Income-tax Officer continued to exercise his territorial jurisdiction it was not legal to transfer any special case to the jurisdiction of the Special Income-tax Officer. It is not a fact that any special case is transferred to the jurisdiction of the Special Income-tax Officer. The fact is that the Commissioner of Income-tax by an order in writing under section 5(4) appointed an Income-tax Officer to perform all the functions of an Income-tax Officer in respect of all classes of income of a certain class of persons in Calcutta, viz., those whose income-tax assessments require, in his opinion, special enquiries, any special scrutiny of accounts, which the ordinary Income-tax Officers having jurisdiction over areas in which their prin-

principal places of business are cannot undertake on account of pressure of ordinary work. The Commissioner of Income-tax selects a number of cases of such persons every year for this Special Income-tax Officer to deal with. The ordinary Income-tax Officers cease to function as Income-tax Officers in respect of this class of persons during the time when the Special Income-tax Officer exercises his jurisdiction over them under Commissioner's order under section 5 (4). There appears to be nothing illegal in this.

S. N. Banerjee, Profulla Chandra Chakraborty and C. C. Bose, for the assesseees.

N. N. Sarkar and Radhabinode Pal, for the Crown.

JUDGMENT

RANKIN, C. J.:—In this case the Commissioner of Income-tax, Calcutta, has referred to the Court under clause (1) of section 66 of the Income-tax Act the question whether “the Special Income-tax Officer” had any jurisdiction over the petitioners’ case within the meaning of sub-section (4) or (5) of the Income-tax Act.

The petitioners have been assessed to income-tax in default of compliance with the requirements of notices directed to them under clause (2) of section 23 and clause (4) of section 22 by a gentleman to whom the name of “Special Income-tax Officer” has been given in view of the provisions of clause (4) of section 23 of the Act. Divers objections were taken to the assessment and an appeal was taken to the Assistant Commissioner which was rejected. An application was then made under section 33 to the Commissioner himself to revise the order of the Assistant Commissioner. In connection with that proceeding, the Commissioner has used his discretion and referred the question to us which I have set out.

Under the provisions of section 23 of the Act and the cognate sections, the person who, in the ordinary course, has to make assessment is an officer called “the Income-tax Officer”, and by section 64 of the Act the place of assessment is defined as the place of the residence of the assessee or where he carries on business or, if more places than one, the principal place of business. The question before us turns upon clause (4) of section 5 of the Act. The officer who, in this case made the assessment, was Babu P. L. Bhattacharyya and the complaint of the assesseees is that he was not the Income-tax Officer of the District in which the petitioners resided, or had their principal place of business though he is a person who has been appointed by the Commissioner of Income-tax under clause (4) of section 5. Now the Commissioner under that section has power given to him by the following words of the clause: “They shall perform their functions in respect of such classes of persons and such classes of income and in respect of such areas as the Commissioner of Income-tax may direct”. For the present purpose we may leave out of account the reference to “classes of income” and the reference to “areas.” So, the power given to the Commissioner is that the Income-tax Officers shall perform their functions in respect of such “classes of persons” as the Commissioner may direct. We have been provided with a copy of the order, dated the 13th December 1927 under which a direction is given by the Commissioner with respect to the Officer in question. It is as follows: “In exercise of the powers conferred on me by section 5 (4) of the Indian Income-tax Act (XI of 1922), I hereby appoint Babu Phanindra Lal Bhattacharyya, Income-tax Officer, to perform all the functions of an Income-tax Officer in respect of those persons in Calcutta whose cases may be made over to him by me from time to time.” The question is whether “those persons in Calcutta whose cases may be made over to him by me from time to time” is

a class of persons within the meaning of clause (4) of section 5. I am clearly of opinion that it is not. It is not possible for any assessee or other person by looking to the definition given in this order to ascertain whether or not his case is one which is affected by it. This order requires a special direction to be given under it from time to time assigning not classes but individual cases to the Officer in question. There may or may not be objections, serious or otherwise to such a course, but I am clear that it is not a course warranted by sub-section (4) of section 5 of the Act.

In these circumstances, it appears to me that we ought to answer the question put to us in the negative.

The result is that the assessment order made upon the petitioners cannot be supported. The petitioners must have their costs of the reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(323) IN THE HIGH COURT OF JUDICATURE AT RANGOON

*Before Sir Benjamin Heald, Kt., Offg. Chief Justice Mr. Justice Chari
and Mr. Justice Brown.*

(2nd August, 1929.)

E. M. Chettyar Firm

.. Assessee*

v.

The Commissioner of Income-tax, Burma

.. Referring Officer

Indian Income-tax Act (XI of 1922), Secs. 31 and 66—Admission of further evidence in appeal—Assessment by Assistant Commissioner to the best of judgment—Duty to record basis of assessment—Enhancement without disclosing materials therefor—Validity of—Findings of fact, when amount to question of law.

The question whether there was any evidence on which the Assistant Commissioner or Commissioner could come to a finding of fact is a question of law. Where the finding of fact was an inference from other facts, the question whether such an inference has been properly drawn is not a question of law.

It is entirely within the discretion of the Commissioner of Income-tax disposing of an appeal whether or not he would admit further evidence at that stage, the appellant having no higher rights than he would have in a civil case under Order 41, Rule 27, Civil Procedure Code.

In disposing of an appeal, the Assistant Commissioner is entitled to make an assessment to the best of his judgment where the assessee did not produce his complete accounts and to enhance the assessment by increasing the income under the source assessed by the Income-tax Officer. In such a case he must give the reasons for and the basis of his assessment for the purpose of enabling the Commissioner to see whether the estimate made was according to the best of the Assistant Commissioner's judgment or wholly arbitrary.

Under the proviso to Sec. 31, it is not necessary to give notice that the Assistant Commissioner proposes to enhance the assessment to any particular figure or to disclose the materials on which the assessment is about to be made and an enhancement of assessment by the Assistant Commissioner without previously disclosing the materials therefor is not illegal.

Case [Civil Reference No. 4 of 1929] stated under Sec. 66(2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma for the opinion of the High Court.

CASE.

Under section 66(2) of the Indian Income-tax Act, 1922, I have the honour to refer to the High Court five questions of law arising out of the orders passed under sections 31 and 32 of the Act in the above named petitioners' appeals in the matter of their assessment for the year 1925-26.

2. The relevant facts are as follows:—

(a) The petitioners are a Hindu undivided family of Puduvayal, Ramnad District, Madras Presidency. They carry on money lending business in different places but the only business with which this reference is concerned is that carried on at Moulmein under the vilasam E. M.

(b) For the year 1925-26 the petitioners returned a loss of Rs. 7,508 and were assessed by the Income-tax Officer, Moulmein, on an income of Rs. 1,00,386 of which Rs. 78,413 was income from the business at Moulmein. The accounting year for the assessment began on the 13th April 1924 and covered therefore the accounts of the new agency which began on the 24th April 1924 and the accounts for the old agency prior to that and which were kept concurrently with the accounts of the new agency.

(c) Against this assessment the petitioners appealed under section 30 of the Act. While dealing with the appeal the Assistant Commissioner was shown both the old agency and the new agency accounts of the petitioners, but as his attention was not at that time directed to the points which threw suspicion on these accounts he did not make that careful examination of the old agency accounts which subsequent events showed to be necessary. When the Assistant Commissioner did become suspicious of the accounts he, in the exercise of his power under section 31 (2), directed the Income-tax Officer to make further enquiry. On the 20th May 1927 the Income-tax Officer submitted a report which afforded strong grounds for believing that the accounts on which the assessment was based were not the full and complete accounts of the petitioners' business at Moulmein.

(d) The grounds for this belief are given in the Assistant Commissioner's appellate order as follows:—“The balance sheet filed by the appellant-concern in connection with the assessment which is the subject of the present appeal showed that the amount of loans outstanding with their customers was Rs. 6,01,569 at the end of Rakthakshi (1924-25), whereas the balance sheet filed in connection with the previous year's assessment showed the amount outstanding at the end of Rudhirothkari (1923-24) as Rs. 9,87,266. There was thus a decrease of over Rs. 3,85,000 in the amount of loans advanced to customers. In the absence of evidence to show that there had been a marked diminution in the business of the appellant-concern this abnormal decrease in the volume of their transactions was extremely suspicious. From a comparison of the details of interest payments for the two years it appeared that a payment of about Rs. 22,000 (Rs. 17,730-7-0 and Rs. 4,214-7-6 respectively) was made under the headings 'M.R.M.V.' and 'Land Purchase Account' in the year Rudhirothkari,

whereas in the year Rakthakshi the payment made on the first account was Rs. 1,427-4-6 only. In other words the capital subscribed by M.R.M.V. had shrunk from over Rs. 2 lakhs in Rudhirothkari to about Rs. 14,000 only in Rakthakshi. As M.R.M.V. are initials denoting various members of the appellant-concern's family an explanation was obviously required of this extraordinary reduction in their capital as shown in the accounts produced. Secondly, there were loans aggregating Rs. 1,34,500 outstanding against one G. M. Lotiah. This amount was transferred to the accounts of the new agency produced before the Department. But the transfer was not effected in a manner which is ordinarily employed. The usual method of recording such a transfer would have been to make a debit entry against Lotiah with a corresponding credit entry in the folio 'Old Account' in the new agency books. But what the appellant-concern did was to make the credit entry in the account of Ahmad Ajam Pippidi instead of in the 'Old Account' folio. Thirdly, in the Pippidi account itself the transfer from the old agency to the new agency was effected by three separate transactions on three different dates instead of by a single transaction which is the usual method. Fourthly, certain transactions with one Mr. Lonsdale were also shown in the account of Ahmed Ajam Pippidi instead of in his own accounts. According to the new agency accounts produced the transactions with Mr. Lonsdale were of recent date and the agent alleged that the appellant-concern had no previous transactions with this gentleman. Documents found in Mr. Lonsdale's possession, however proved that he had been dealing with the appellant-concern for many years previously. Among these documents were two receipts for Rs. 3,000 and Rs. 2,000 respectively, granted by the agent and by the proprietor's son. The particular transactions to which these receipts related did not find a place in the accounts produced. These receipts moreover proved that Mr. Lonsdale's dealings were with the appellant-concern and not with Ahmad Ajam Pippidi. The above facts showed that the Ahmad Ajam Pippidi account was probably a fictitious account. Fifthly, the accounts of the O.R.M. firm at Theinzeik in the Thaton District showed that on the 17th September 1924 a sum of Rs. 5,000 was borrowed from the appellant-concern at Moulmein. The pro-note was executed not in the name of E.M., but in the name of Puduvayal K.V.M. through Muna Vina. Vina stands for Visvanathan Chettyar, the proprietor of the E.M. concern; Muna stands for his son Muthappa Chettyar; while K denotes Kadaing Meya Kwin in which their paddy lands are situated. This loan, according to the accounts of O.R.M., was repaid with interest of Rs. 753-8-6 to the appellant-concern at Moulmein on the 13th February 1927. The agent of the appellant-concern admitted collecting this loan himself, but there was no record of it in the accounts produced before the Income-tax Officer. Sixthly, from a report received from the Income-tax Officer, Karaikudi, it appeared that the head-quarter's accounts of the appellant-concern contained two interest payments of Rs. 8,569-7-6 and Rs. 1,104 made during the accounting year Rakthakshi (1924-25) to the appellant-concern at Moulmein. But in the accounts of the latter produced at Moulmein only the first item of interest was recorded. Seventhly, loans were admittedly advanced, under the vilasams K.V.M., and N.V.M., from the proceeds of the paddy lands in the Thaton District owned by the proprietors of the appellant-concern. The initials V. and M., as shown above, stand for the proprietor Visvanathan Chettyar and his son Muthappa Chettyar. The prefixes K. and N. undoubtedly denote Kadaing Meya and Nallichan, the kwins in which the lands are situated. The transactions connected with these loans were made through the agency of the appellant-concern at Moulmein. Yet there was no record of these transactions in the accounts of the appellant-concern produced before the Department. All the above facts constituted grounds for believing that the accounts of the new agency of the appellant-concern which were produced before the Department did not fully cover all the transactions carried

on by the appellant-concern during the accounting year Rakthakshi (1924-25) and that other accounts must have been maintained in addition to those accounts."

(e) The Assistant Commissioner in order to test the accounts on which the assessment was based accordingly issued a notice to the petitioners for the production of the following accounts:—(1) All the new agency accounts commencing from the 24th April 1924. (2) All the old agency accounts (i.e., the accounts of the agency prior to the new agency). (3) All the accounts showing the transactions with the C.R.M.S., concern, Rangoon, for the year Rakthakshi 1924-25. (4) All the accounts showing the investments in paddy lands in the Thaton District, the produce from them every year since 1923-24 and the investments made in other Chettyar concerns from the sale proceeds of such produce.

(f) On the 13th July 1927 the Assistant Commissioner passed an order directing the Income-tax Officer to examine these accounts when produced and report on them.

(g) Of these accounts only No. (1) was produced; No. (2) was said to have been lost at the Rangoon wharf by the person who was bringing it from Madras; as to Nos. (3) and (4) which, for convenience sake, are called hereafter the R.M.P.R., accounts, it was alleged that the transactions and investments mentioned concerned the family of Visvanathan's deceased brother Periyannan and that the petitioners had nothing to do with them.

(h) The Assistant Commissioner gave the petitioners a further hearing on the 28th September 1927 when the petitioner's advocate, their auditor and their Moulmein agent were present. The agent said that he hoped to be able to recover the accounts that had been lost if he were given two months' time; he also agreed to produce the other accounts called for, i.e., the R.M.P.R., accounts Nos. (3) and (4) above and in addition all the headquarters accounts kept at Pudukkottai. A notice was accordingly issued to the agent for the production of accounts Nos. (1) and (2) and the headquarters accounts; and at the request of the agent a separate notice was issued to R.M.P.R., Sivagami Achi for the production of accounts Nos. (3) and (4). Five sets of accounts in all were therefore called for.

(i) On the 10th December 1927, the next hearing took place and on that date the petitioners produced only the new agency accounts [No. (1) above] which they had produced on the previous occasion.

(j) On the 15th December 1927 the Assistant Commissioner sent to the advocate of the petitioners a note specifying the points which the petitioners were required to explain. A copy of this note is attached and marked A.*

(k) On the 23rd December 1927 there was a further hearing and on the 3rd January 1928 the Assistant Commissioner called on the petitioners to show cause why the assessment should not be enhanced. On the 14th March 1928 the Assistant Commissioner came to the finding that the petitioners had maintained two sets of accounts for the accounting year but produced only one set before the Income-tax Department and that therefore the assessment made by the Income-tax Officer on the incomplete accounts was inadequate. He accordingly passed orders enhancing the assessment under the head "Burma business" from Rs. 78,413 to Rs. 2,00,000, which was an estimate of the petitioners' income at Moulmein to the best of his knowledge and belief. Copy of this order is attached and marked B.*

(1) Against this enhancement the petitioners appealed under section 32 of the Act to the Commissioner. During the course of the proceedings before him the Commissioner refused to admit the R.M.P.R., accounts in evidence at that stage. The Commissioner confirmed the enhancement made by the Assistant Commissioner. A copy of his order is attached and marked C.*

3. The five questions which I am asked to refer are as follows. I arrange them for convenience in a different order from that in which they are stated by the petitioners. The petitioners originally asked me to refer some fourteen questions, but after discussion and correspondence with their advocates they have agreed that the five questions now referred cover all the points in issue.

Question 1: "Whether there was evidence on which the Assistant Commissioner and the Commissioner could find that the books of account on which the assessment of the Income-tax Officer was based were not the full and complete accounts of the petitioners' business for the year."

Question 2: "Whether in these assessment proceedings the Income-tax authorities were entitled to insist on the production in Burma of the petitioners' accounts which were maintained in Pudukkottai."

Question 3: "Whether the Commissioner erred in law in refusing to admit the R.M.P.R., accounts at the hearing of the appeal before him."

Question 4: "Whether the enhancement of the petitioners' income under the head 'Burma business' made by the Assistant Commissioner was such an enhancement as is contemplated by section 31 of the Income-tax Act, 1922, and in accordance with the provisions of that section."

Question 5: "Whether even assuming that the petitioners wilfully failed to produce the accounts, the Assistant Commissioner acted illegally in enhancing the assessment in respect of their Burma business to two lakhs of rupees without disclosing to them the materials he had before him in support of such assessment, so as to give them an opportunity to rebut or disprove such materials."

4. As to the first question I would submit that it is the Assistant Commissioner's finding only which is in issue since all that the Commissioner did was to uphold it on appeal. The only evidence to be considered therefore is the evidence before the Assistant Commissioner with the exception of certain affidavits filed before the Commissioner.

The evidence on which the finding is based is set out and examined at length in the orders of the Assistant Commissioner and of the Commissioner copies of which are attached and marked B and C. I need only therefore state it as briefly as possible here. The first point is the reluctance of the petitioners to produce the accounts called for. The old agency accounts were first said to have been lost and later the petitioners' agent said he hoped to recover them. Their loss was not reported to the Police or to the shipping or wharf authorities and there is no evidence of any attempt to recover them. In the circumstances it was reasonable to conclude that they were not lost at all. The R.M.P.R., accounts, if they existed as separate accounts, were admittedly under the control of E. M. Visvanathan's son Muthappa and could have been produced if the petitioners wished to produce them. Their refusal to do so strengthens the inference that the Moulmein accounts shown to the Income-tax Officer were not the true and complete accounts of the business. The refusal to produce the headquarters accounts which the agent agreed to obtain was persisted in up to the last moment until it was too late to produce them. This again, strengthens the inference against the accounts on which the assessment was based.

The great decrease in the amount of outstanding loans and the entries in the new agency accounts relating to Lotiah, Lonsdale and Pippidi are explained by the petitioners by alleging that there was a partition between E. M. Visvanathan and his son on the one hand and the widow of his brother Periyannan on the other hand and that she has now a separate estate called R.M.P.R. This is such a convenient way of explaining transactions which *prima facie* ought to appear in the E.M. accounts but do not (by saying that such transactions relate to the R.M.P.R. estate) that it is naturally open to the greatest suspicion. The first mention of this partition in the proceedings occurs in the agent's petition of the 26th August 1927 in which he states that the family was divided in the life-time of Periyannan Chettyar, who died in March 1920. That petition was not submitted until after the petitioners knew that their accounts were under suspicion. But in an affidavit filed subsequently before the Commissioner E.M. Visvanathan states that the partition took place in August 1923 and that it was due to differences between himself and his brother Periyannan Chettyar's widow. This discrepancy is difficult to understand since the agent had been in the employ of the petitioners for about 15 years and would naturally know when a partition had taken place; and the statement was not made at random since it was made in writing and was supplemented by the oral statement that previous to July 1924 there were no separate accounts since transactions of R.M.P.R. were too few to require accounts. He also admits that prior to the accounting year the capital alleged to be R.M.P.R., capital stood in the name of M.R.M.V., i.e., Visvanathan and his son. The agent also states that the partition was not reduced to writing whereas E. M. Visvanathan states that it was reduced to writing. An attempt was made by the petitioners to have the R.M.P.R., estate assessed separately at Karaikudi when they came to know that the accounts produced in Burmah were suspect, but the Income-tax Officer there, after investigating the facts, came to the conclusion that there was no partition. This finding is, I submit, an important piece of evidence as it was elicited by petitioners' attempt to get a separate assessment at Karaikudi.

The agent's first explanation of the manipulation of Lotiah's account was that it was not taken over by the new agency as it was not considered good. Subsequently an entirely different explanation was given, viz., that Lotiah's transactions were with the R.M.P.R., and when the debt became doubtful it was transferred to E. M., as it would not look well if R. M. P. R. suffered loss on transactions with Lotiah who was vouched for by E.M. As to why the corresponding credit was made to the account of Pippidi it was explained that Pippidi was looking after the business of R.M.P.R., and the credit was therefore made in his name. Now Pippidi is a man of straw who has admitted that he is supported by his father and that he had no dealings with the E.M. since 1923. Yet the agent stated in May 1927 that two sums in cash of Rs. 2,000 and Rs. 2,800 had been taken from Pippidi in 1925. Finally it was admitted by the petitioners' advocate before the Commissioner that the Pippidi account was a purely fictitious account invented with the object of concealing from the Income-tax authorities the existence of the R.M.P.R. estate. In regard to Lonsdale's transactions too it is perfectly clear that the petitioners' agent has not been telling the truth. Up to the final hearing of the appeal before the Assistant Commissioner he could or rather would give no explanation of this account other than that it possibly had some connection with Pippidi. Only at the final hearing was it clearly stated that Lonsdale's transactions were to be found in the R.M.P.R., accounts. The whole explanation as to the manipulation of these accounts being due to the partition between E.M., and R.M.P.R., is too improbable to be taken seriously. On the petitioners' own showing they have been making fictitious entries in their accounts with the object

of concealing information from the Income-tax authorities. This affords another reason, if one were wanted, for viewing their accounts with the gravest suspicion and putting them to strict proof that these accounts are the true and complete accounts of their business.

The omission of the loan to O.R.M. firm, Theinzeik, from the petitioners' accounts is explained by saying that it also is an R.M.P.R., transaction. But this explanation does not get over the fact that the loan was made in the names of E. M. Visvanathan Chettyar and his son Muthappa and was repaid to the E.M. firm (petitioners), Moulmein.

It will, I think, be admitted that, in view of the irregular and most unusual entries in and omissions from the accounts which were before the Income-tax Officer and the failure to produce the accounts called for by the Assistant Commissioner, the appellants were bound, if they wanted the Assistant Commissioner to accept their accounts as the basis of his decision on the appeal, to prove the partition which was the foundation of their whole case. But the only evidence for the partition—if it can be called evidence in the circumstances—put before the Assistant Commissioner was the statement of the petitioners unsupported by any corroboration whatever. They cannot complain of lack of time or opportunity since from first to last the appeal proceedings before the Assistant Commissioner lasted nearly two years. And yet it was not until the case came before the Commissioner on appeal that the petitioners produced affidavits in support of the partition and offered to produce the R.M.P.R. accounts. Meanwhile the petitioners had steadily refused to produce before the Assistant Commissioner the evidence which he wanted, *viz.*, the various sets of accounts already set forth; and had produced no evidence whatever except their own statement in support of their fundamental contention that there was a partition. I submit that, in the circumstances and on the facts, the only conclusion which the Assistant Commissioner could have come to or at least the obvious conclusion was that the accounts which were before the Income-tax Officer were not the true and complete accounts of the petitioners' business at Moulmein for the accounting year.

That was the position when the Assistant Commissioner enhanced the assessment and subject of course to the contrary view being held by the Hon'ble Judges on Question 3. I maintain that that is the position on which this question should be decided. The petitioners had every opportunity to put their case before the Assistant Commissioner and since they refused to support their mere statement by any corroborative evidence I submit that the evidence offered by them subsequently before the Commissioner should be ignored.

On this question therefore I submit that there was evidence on which the Assistant Commissioner could find that the accounts before the Income-tax Officer were not the true and complete accounts of the petitioners' Moulmein business for the accounting year and that the Commissioner was justified in upholding that finding.

5. On the second question it was contended on behalf of the petitioners that the Assistant Commissioner was not entitled to insist on the production in Burma of the accounts kept at Pudukkottai; but that he should have had them examined by the Income-tax authorities of that District. In their petition of appeal the petitioners did not go so far as to say that the Assistant Commissioner acted illegally in insisting on the production of these accounts. All that they said was that he acted irregularly and unjustly. I submit, however, that the only point for consideration in regard to this question is whether the Assistant Commissioner had the power to call for these accounts. Whether he should have studied the convenience of the petitioners is another matter and certainly

not a question of law arising out of the proceedings. The Assistant Commissioner's powers in this respect are conferred by section 37 and that section imposes no such limitation as is contended for by the petitioners. In my opinion therefore the answer to this question is 'Yes'.

6. My opinion on the third question is that the Commissioner did not err in law in refusing to admit these accounts on appeal. The Commissioner was acting under section 32 which, so far as the appellant's opportunity of putting his case is concerned, prescribes only that the Commissioner should give the appellant an opportunity of being heard. To say that this includes the obligation to admit any fresh evidence that the appellant cares to put in is to strain the meaning of the words which are plain and clear; and on the particular facts of this case such an interpretation would be manifestly absurd since the petitioners had every opportunity of producing these accounts before the Assistant Commissioner and did not do so. I submit that in income-tax proceedings the law gives the appellant no more right to put in fresh evidence on appeal than is given to an appellant in a civil appeal by Order 41, Rule 27, of the Civil Procedure Code.

7. As to the fourth question the petitioners contended that the enhancement by the Assistant Commissioner is illegal on two grounds:—(a) that section 31 gives the Assistant Commissioner no power to ignore the materials which were accepted and acted upon by the Income-tax Officer and to make a summary assessment which is a mere estimate; (b) that section 31 gives the Assistant Commissioner no power to assess income which according to him was not included in and not covered by the assessment appealed against. Section 31 lays down no conditions precedent to an order of enhancement. There is nothing whatever in the section which would indicate that the enhancement must be based on the materials before the Income-tax Officer. On the contrary, sub-section (2) which provides for a further enquiry negatives this view. Nor is there anything in section 31 which prevents the Assistant Commissioner from making an enhancement which is only an estimate. If the evidence produced by the appellant is held to be false or incomplete and he is unwilling to state the full facts as to his income, I submit that the only course open to the Assistant Commissioner is to make an estimate to the best of his judgment.

The second argument on this question is in my opinion equally fallacious. If this argument were correct it would not be possible to make an enhancement under section 31 in any case. For what the Assistant Commissioner has done in this case is to enhance the income of the Moulmein business and not to bring under assessment a new source of income or income from a new business the existence of which was not known to the Income-tax Officer at the time of making the assessment.

On this question therefore I am of opinion that the enhancement was such an enhancement as is contemplated by section 31 of the Income-tax Act and in accordance with the provisions of that section.

8. On the fifth question the petitioners maintain that before the enhancement was made the Assistant Commissioner was bound in law to disclose to them the materials on which he came to the conclusion that their income from Burma business was Rs. 2,00,000 and not Rs. 78,413 as determined by the Income-tax Officer from the petitioners' accounts. I fail to understand how this question is raised in view of the many opportunities which the petitioners had of producing all relevant accounts before the Assistant Commissioner and satisfying him that the set of accounts produced before the Income-tax Officer were the true and complete accounts of their business. Moreover, the particular points which led the Assistant Commissioner to believe that the petitioners had with-

held their true accounts from the Income-tax Officer were clearly put to the petitioners before the enhancement was made and yet they still failed or refused to produce the accounts called for or any other evidence whatever which would have satisfied him that his belief was not justified. In the circumstances, the only course open to the Assistant Commissioner was to make an estimate of the petitioners' income from their business and I submit that the estimate made by him cannot be impugned. On this question therefore my opinion is that the Assistant Commissioner did not act illegally.

C. H. Gaunt, for the Crown.

A. J. Darwood with *Foucar*, for the Assesseees.

JUDGMENT

This is a reference by the Commissioner of Income-tax of Burma. The facts of the case are fully and clearly set out in the reference and it is unnecessary to give them in detail. Briefly stated they are that the E. M. Chettyar firm, which was carrying on business in Moulmein, was assessed for the year 1925-26 by the Income-tax Officer on an income of Rs. 1,00,386 of which Rs. 78,413 was income from the Moulmein business. The assessee had returned a loss of Rs. 7,508. The Chettyar firm appealed against the assessment under section 30 of the Act; and the Assistant Commissioner, during the hearing of the appeal, became suspicious of the accounts. He thereupon directed the Income-tax Officer to make a further enquiry. The result of the enquiry was submitted to him and for the purpose of testing the accounts on which the assessment was based he issued a notice to the Chettyar firm to produce four sets of accounts. Of these accounts, one set was produced before him; one set was said to have been lost at the Rangoon wharf when it was being brought over from Madras, and the two other sets were alleged to be the accounts of R.M.P.R. which is said to be a separate business carved out of the E. M. firm by an arrangement with the widow of a deceased partner and to have been created for the purpose of being allotted to the share of a son whom, it was intended, the widow should adopt to her deceased husband.

At a later hearing the Assistant Commissioner was told that the agent of E. M. firm hoped to recover the accounts lost at the wharf and he also agreed to produce the R.M.P.R. accounts which were kept at Pudukkottai and not in Burma. Later the Assistant Commissioner sent to the advocates of the Chettyar firm a note wherein he asked them to explain certain points. The explanation was either not forthcoming or was not satisfactory to the Assistant Commissioner, who on the 3rd January 1928 issued a notice to the Chettyar firm to show cause why the assessment should not be enhanced. This he was bound to do under the proviso to section 31 of the Act. He later enhanced the assessment under the head of Burma business from Rs. 78,413 to 2 lakhs of rupees. In his appellate judgment the Assistant Commissioner stated that to the best of his information and belief the net taxable income of the E. M. concern at Moulmein was not less than two lakhs. The Chettyar firm then took up the matter in appeal to the Commissioner of Income-tax, who dismissed the appeal. The Commissioner was then asked to refer to this Court the following questions said to arise out of the case:—

1. Whether there was evidence on which the Assistant Commissioner and Commissioner could find that the books of account on which the assessment of the Income-tax Officer was based were not the full and complete accounts of the petitioners' business for the year.

2. Whether in these assessment proceedings the Income-tax authorities were entitled to insist on the production in Burma of the petitioners' accounts which were maintained in Pudukkottai.
3. Whether the Commissioner erred in law in refusing to admit the R.M.P.R. accounts at the hearing of the appeal before him.
4. Whether the enhancement of the petitioners' income under the head "Burma business" made by the Assistant Commissioner was such an enhancement as is contemplated by section 31 of the Income-tax Act, 1922, and in accordance with the provisions of that section.
5. Whether even assuming that the petitioners wilfully failed to produce the accounts, the Assistant Commissioner acted illegally in enhancing the assessment in respect of their Burma business to two lakhs of rupees without disclosing to them the materials he had before him in support of such assessment, so as to give them an opportunity to rebut or disprove such materials.

The 2nd question has not been pressed before us in view of our judgment in another case* in which a similar point arose, where we decided that it was competent for the Commissioner to call for the production of books which were maintained outside British India.

We shall now consider the other questions *seriatim*.

Question 1 seems to be a question of fact disguised as a question of law. It has been repeatedly held that under section 66 of the Income-tax Act only questions of law can be referred to the Court. We have no jurisdiction to consider any question of fact and the finding of the Assistant Commissioner or the Commissioner on questions of fact is final. It has, however, been held that the question whether there was any evidence on which an Assistant Commissioner or the Commissioner could come to a finding of fact is a question of law. If there was any evidence upon which it was reasonably possible for the Commissioner to come to the conclusion at which he arrived, the High Court will not consider whether on that evidence that finding was correct, because the High Court is not a court of appeal in respect of findings of fact arrived at by the Commissioner. (See the *American Thread Co. v. Joyce*(1) and the cases discussed therein). Even where, as in this case, the finding of fact is an inference from other facts the question whether such an inference has been properly drawn is not a question of law. An inference of fact drawn from other facts admitted or proved is itself a finding of fact. Thus in *Queen v. Special Commissioners of Income-tax*(2) the Master of Rolls in considering the question whether the Commissioners were entitled on the ground of the assessee not producing his books coupled with certain other facts to draw the inference that certain items in a schedule furnished by the assessee were wrong said:—"It is a question of the true inference which they had to draw as a matter of evidence upon the facts which they had in evidence before them. But to draw an inference of fact from evidence before you is not a question of law at all. The inference is a question of fact just as much as the direct evidence of fact, and it would be an appeal against facts, which we are not entitled to entertain, and consequently there can be no *Mandamus*. To say that these gentlemen did not assume to hear and determine the case is idle. They did. But the question is whether they did it by the exercise of something which was beyond their jurisdiction. I say, if

(1) 6 Tax Cas. 1.

(2) 8 Tax Cas. 289.

*Reported as *Somasuudaram Chettiar v. Commissioner of Income-tax, Burma*, 4 I.T.C. 11.

that is a question of fact, the mere question of whether they appreciated the evidence rightly or not, and whether they drew a right inference of fact, is not the subject matter of a *Mandamus* at all. There would be an appeal if there was an appeal, but there is none."

In this case, the Assistant Commissioner, from the fact of non-production of certain books which the Chettyar firm was ordered to produce coupled with other facts mentioned in his order, came to the conclusion that the books of account on which the assessment was based were not the full and complete accounts of the petitioner's business for the year of assessment. This is a finding of fact and there was ample evidence from which the Assistant Commissioner could draw the inference that the books produced were not the full and complete accounts of the business. Whether on the evidence we would come to the same conclusion or not is a question which does not arise.

It has been urged before us that as there was a partition among the members of the E. M. family there was justification or, at all events, excuse for the E. M. firm not producing the R.M.P.R. accounts, but the question whether this alleged partition took place and whether it afforded any excuse for the non-production of the books before the Assistant Commissioner are questions of fact. They are pieces of the evidence on a consideration of the whole of which the Assistant Commissioner arrived at his finding of fact. We therefore answer Question 1 in the affirmative and hold that there was evidence on which the Assistant Commissioner could come to the conclusion at which he arrived.

Question 3. After the Assistant Commissioner had enhanced the assessment, and when the matter was taken up in appeal to the Commissioner, the Chettyar firm offered to produce the R.M.P.R. accounts. These ought to have been produced before the Assistant Commissioner and it was entirely in the discretion of the Commissioner whether or not he would admit further evidence at that stage. The Commissioner rightly remarks that an appellant in income-tax proceedings has no higher right in adducing fresh evidence in appeal than he would have in a civil case under Order 41 Rule 27 of the Civil Procedure Code. The Chettyar firm had had ample opportunity of producing the R.M.P.R. accounts before the Assistant Commissioner and therefore we answer this question in the negative and hold that the Commissioner did not err in law in refusing to admit those accounts at the hearing of the appeal.

As regards *Question 4*, it was suggested before us that the Assistant Commissioner had arrogated to himself the power of assessing to the best of his judgment which is given only to the Income-tax Officer under section 23(4) of the Act. From the reference submitted by the Commissioner the argument on this question before him seems to have been that section 31 does not give the Assistant Commissioner power to ignore the materials accepted and acted upon by the Income-tax Officer and to make a summary assessment and that it does not give the Assistant Commissioner power to assess on income which according to him was not included in and not covered by the assessment appealed against.

As regards the second of the two arguments above stated we are in agreement with the Commissioner; if the argument were sound, it would mean that the Assistant Commissioner could not enhance the assessment. In any case, the Assistant Commissioner did not in fact assess any new source of income or the income of a new business. He merely enhanced the income of the Moulmein business to two lakhs of rupees.

As regards the first part of the argument, it is true that where the Assistant Commissioner is satisfied that the account books produced before him are not the complete accounts and the assessee does not produce his accounts to enable the Assistant Commissioner to arrive at a correct estimate of the income,

the only course open to the Assistant Commissioner is to make an estimate of the income to the best of his judgment, but this does not mean that the Assistant Commissioner acts under section 23(4) of the Act. But in a case like the present he is entitled to make an assessment to the best of his judgment. He must of course give the reasons and the basis of his assessment for the purpose of enabling the Commissioner to see whether the estimate was made according to the best of the Assistant Commissioner's judgment or it was wholly arbitrary. In his appellate order the Assistant Commissioner says "To the best of my information and belief the nett taxable income of the appellant-concern's business at Moulmein during the accounting year was not less than two lakhs of rupees. It is highly improbable that any assessee and least of all an astute Chettyar money lender, would go to the length of maintaining a double set of accounts and concealing part of his income unless the stakes were worth the hazard. Under section 31 (3) (a), therefore I enhance the assessment under the head "Burma Business" from Rs. 78,413 to Rs. 2,00,000". It will thus be seen that, though the Assistant Commissioner states that the assessment is to the best of his information and belief, he does not mention the facts and figures on which his assessment was based. In matters of assessment where such wide powers are vested in the Income-tax Officials, it is highly desirable that they should avoid even a semblance of arbitrary action. Our answer to Question 4 therefore is that if the enhancement of the Assistant Commissioner is based on materials from which he could reasonably conclude, though only as a rough estimate, that two lakhs of rupees were the income of the Moulmein business then the enhancement was legal; if, on the other hand, the enhancement was wholly arbitrary and based upon no materials, it was illegal. In view of this answer the proper course for the Commissioner to adopt will be to call upon the Assistant Commissioner to give the grounds on which he based his assessment and the Commissioner as an appellate tribunal can then consider whether the enhancement was justified on these materials. If in his opinion there were materials on which the Assistant Commissioner could arrive at the enhanced figure there is an end of the matter, since there is no further appeal and we cannot enter into the questions of fact, namely, as to the sufficiency of those materials for the conclusion arrived at.

Question 5: On this question the argument before us took an apparent different turn from that before the Commissioner. It was argued, first, that the Assistant Commissioner was bound in law to disclose the materials on which he came to the conclusion that two lakhs of rupees were the income of the Burma business in order to enable the Chettyar firm to meet the case. The proviso to section 32 contemplates merely a notice by the Assistant Commissioner that he proposes to enhance the income. It is not necessary under that proviso to give notice that the Assistant Commissioner proposes to enhance the assessment to any particular figure or to disclose the materials on which the enhancement is about to be made. As we have stated in the answer to the last question, it is desirable that the Assistant Commissioner, in his order enhancing the assessment, should mention the basis of the enhanced assessment but this is merely for the purpose of satisfying the appellate tribunal that the assessment was not arbitrary. It was open to the Chettyar firm when notice was issued under the proviso to section 32 to show cause against the enhancement and to convince the Assistant Commissioner that if he did enhance the income it should not be above a certain figure. Our answer to Question 5 is therefore that the Assistant Commissioner did not act illegally in enhancing the assessment without previously disclosing the materials on which he based the enhanced assessment.

Each party will bear his own costs in respect of this reference.

(324) IN THE HIGH COURT OF JUDICATURE AT PATNA

Before Mr. Justice Das, Mr. Justice Kulwant Sahay and Mr. Justice Wort.

(7th August, 1929.)

Raja Raghunandan Proshad Singh and another .. Assesseees
v.

The Commissioner of Income-tax, Bihar and Orissa .. Referring Officer.

Indian Income-tax Act (XI of 1922) Sec. 10—Money-lending business—Loans on mortgages providing for compound interest—Purchase of properties by mortgage in execution of mortgage decrees—Income therefrom, when realised—Purchase, if capital transaction—Proper basis of computation of assessable income—Claim for deductions.

The assesseees carrying on money-lending business, in 1894 lent a sum of Rs. 2 lakhs on a mortgage of the Srinagar Raj and in 1904 advanced a further loan of 3 lakhs and obtained a mortgage for Rs. 7,33,135 which included the sum of Rs. 4,33,135 being the principal and interest due under the mortgage of 1894. In 1912 another sum of Rs. 3 lakhs was advanced by the assesseees on a second mortgage of the Raj. The mortgage deeds provided for interest being calculated half yearly and added on to principal. In execution of decrees obtained in 1917 on the mortgages of 1904 and 1912 the assesseees on the 19th November, 1924 and 31st January, 1925, purchased the mortgaged properties in court auction for Rs. 25,65,100, the assesseees' claim under the decrees amounting to Rs. 27,13,379. Sale certificates were issued on the 18th and 21st December 1925 and possession was obtained by the assesseees on 30th September, 1926.

On an assessment to income-tax for the year 1926-27 on a sum of Rs. 15,53,033 being the purchase price less the cost, charges, expenses up to the sale, and the capital sums originally advanced, the assesseees contended that the interest under the mortgages became capital under the terms of the bond and ought to have been assessed, if at all, as it accrued due, that interest under the bond of 1894 extinguished by the mortgage of 1904 was no longer assessable and that the purchase of the properties was a capital transaction. The assesseees further claimed to deduct certain sums of money paid by them into Court as security for the claim of a third party over the properties purchased, as well as the amount of decree obtained against them by a prior mortgagee and expenses incurred in taking delivery of possession and effecting mutation of names and to compute their income on the basis of Rs. 17,13,701, being the valuation of the properties by the Civil Court Commissioner. A further contention was raised that the profits from the purchase of the mortgaged property were received by the assesseees on the dates of the court sales prior to the previous year 1925-1926. The assesseees kept their accounts on cash basis and did not show actual realisation of interest at any time.

On a reference to the High Court under Sec. 66(2) of the Income-tax Act

Held, (1) that on the basis of assesseees' accounts, the mortgage income was assessable as having accrued in the account year and that there was no capitalisation of interest or extinguishment of the bond of 1894 in the later bond of 1904,

(2) that the deductions claimed were not allowable and that the price paid by the assesseees represented the true valuation of the properties,

and (3) that the transaction of purchase was not a capital transaction,

(4) *that the profits were realised by the assesseees on the dates when the court sales became absolute and not on the sale dates.*

On a reference by the Commissioner of Income-tax under Sec. 66(1)

HELD, that on a purchase by the mortgagee of mortgaged properties in execution of a mortgage decree, profits for income-tax purposes must be taken to be what is left over of the total sum realised after satisfaction of principal and costs.

Case [Miscellaneous Judicial Case No. 60 of 1928] stated under Sec. 66 (1) and (2) of the Indian Income-tax Act, (XI of 1922) by the Commissioner of Income-tax, Behar and Orissa, for the opinion of the High Court.

CASE.

In the year 1926-27, the Income-tax Officer, Monghyr, made an assessment under section 23(3) of the Income-tax Act on Raja Raghunandan Prasad Singh, M.L.A., and Raja Deokinandan Prasad Singh, M.L.C., of Monghyr (hereinafter referred to as assesseees) on an income of Rs. 17,02,321 of which Rs. 16,23,459 represents the income which was held by the Income-tax Officer to have been received by the assesseees in the previous year as the result of execution and satisfaction of certain mortgage decrees against the proprietors of the Srinagar estate. The Assistant Commissioner on appeal reduced the assessed income to Rs. 15,53,033 by his order dated 23-5-27 and the assesseees then filed before me an application for reference on certain points of law or alleged points of law. These questions, as framed by the assesseees, and set out in their applications, overlapped considerably and at the time of hearing they reduced the number of questions of law to 7, and I shall discuss these after setting out the history of the case.

2. Kumar Srinand Singh who at one time was the sole proprietor of the Srinagar estate had two wives, by the first of whom he had one son Kumar Nityanand Singh, and by the second two sons, Kumar Kamlanand Singh and Kumar Kalikanand Singh. As the result of a partition effected in the year 1892, Kumar Nityanand got one-third share in the property, the other two-thirds share passing to Kumars Kamlanand and Kalikanand jointly. In the year 1894 (1301 F.S.) Kumar Nityanand Singh borrowed a sum of two lacs from the predecessor in interest of the assesseees in this case and executed a mortgage bond in his favour mortgaging his entire one-third share in a certain portion of the property which he had acquired by partition. This Kumar Nityanand 5 years later (1306 Fasli) borrowed Rs. 3-1½ lakhs from the Rajas of Baneli executing a mortgage bond in their favour. On the basis of this mortgage bond, the Rajas of Baneli filed a suit and obtained a mortgage decree dated 11-3-02 against Kumar Nityanand for a sum of Rs. 4,57,159. The other two Kumars, Kamlanand and Kalikanand purchased this mortgage decree from the Baneli Raj for a consideration of 5 lakhs, but as they were not in a position to pay ready money they executed a mortgage bond for 5 lakhs in favour of the Rajas of Baneli on the same date on which the purchase was effected, namely, 12th September 1903. On the 20th October 1903, Kumar Kamlanand and Kumar Kalikanand purchased by Kebala the one-third share of Kumar Nityanand in the Srinagar estate and from the date of purchase they came into possession of that share.

3. Up to the 18th July 1904 assesseees' dues on the bond for 2 lakhs taken from Kumar Nityanand in 1301 Fasli amounted to Rs. 4,33,135, while the dues of the Baneli Rajas on the bond of 5 lakhs dated the 12th September 1903 amounted to Rs. 5,25,815. As the assesseees' predecessor in interest and also the Baneli Rajas threatened to bring suits for realization of their dues, at this time the two Kumars, Kamlanand and Kalikanand paid to the Baneli Rajas

Rs. 815 from their own pocket and borrowed from the predecessor in interest of the assessee a further sum of 3 lakhs which they also made over to the Baneli Rajas and for the balance of amount due to the Baneli Rajas viz., Rs. 2,25,000, the two Kumars Kamlanand and Kalikanand executed a fresh mortgage bond dated the 18th July 1904. Thus, they satisfied the entire debt due to the Baneli Rajas arising out of the bond for 5 lakhs executed on the 12th September 1903.

4. The amount due to the predecessor in interest of the assessee on the bond for 2 lakhs up till the 18th July 1904 was Rs. 4,33,135 as stated above including interest and principal while further the assessee's predecessor in interest had advanced 3 lakhs in cash. The total sum due to assessee's predecessor in interest was therefore Rs. 7,33,135 and for this sum Kumars Kamlanand and Kalikanand and Kamalanand's two minor sons, Gananand and Ambikanand through their father and guardian Kamlanand, executed a mortgage bond on the 18th July 1904. This was the bond in suit in Case No. 464 which has resulted in a decree and execution on behalf of the assessee and the profits arising out of which have been taxed in the present case.

5. The 2nd mortgage bond on which suit No. 465 was based is dated the 7th November 1912. The circumstances in which this suit rose are as follows: The total amount due to the Baneli Rajas on the mortgage bond of Rs. 2,25,000 dated the 18th July and referred to above amounted to Rs. 3,34,000 on the 7th November 1912. At this time (November 1912) the Baneli Rajas were contemplating the filing of a suit for recovery of their dues and to satisfy the said debt Kumar Kalikanand (Kamlanand being then dead) for self and as Karta of the joint family borrowed from assessee's predecessor in interest a sum of 3 lakhs and executed a mortgage bond in his favour on that date (7th November 1912) and paid that sum to the Baneli Rajas, thus satisfying the entire debt due to them on their bond of 18th July 1904.

6. The above mortgage suits in which assessee was plaintiff and the proprietors of the Srinagar estate defendants were tried jointly and a decree was passed in favour of the assessee on the 22nd December 1917 and the judgment of the Subordinate Judge was upheld on appeal to the High Court and the Privy Council. The mortgaged property was put to sale and bought in by the assessee on 19-11-24 and 31-1-25 while confirmation of sale took place on 18-12-25 and 21-12-25, that is, in the "Previous year" 1925-26 on the income of which assessment was made in this case.

7. The second mortgage in favour of the assessee is of the year 1904 and the third is of the year 1912. It appears that the proprietors of the Srinagar estate had mortgaged the whole estate including the portion covered by the appellants' mortgages to the Rajas of Baneli for seven lakhs on the 29th April 1910 and the Baneli mortgage was therefore subsequent in date to the 2nd mortgage of the assessee, but prior to the 3rd mortgage. In the bond of the 3rd mortgage, there was a covenant that the lien of the bond of the 1904 mortgage was to be kept intact by this subsequent mortgage of 1912, this clause being inserted because the Baneli Rajas held another mortgage for Rs. 2,25,000 against the Srinagar estate the date of which was exactly the same as that of the 2nd mortgage in favour of the appellants, namely, the 18th July 1904 and as a matter of fact the 3rd mortgage in favour of the appellants was executed by the proprietors of the Srinagar estate to enable them to raise money to pay off the Baneli mortgage of 1904. The Baneli Raj, however, filed a suit in 1923 on the basis of the mortgage bond of 1920 making the estate and the assessee co-defendants. In this suit assessee contended that their mortgage of 1912 was prior to the mortgage of 1910 of the plaintiff, as by the covenant in the mortgage of 1912 the rights of the Baneli Raj in the 1904

bond were transferred to the assesseees. The court however held otherwise and on the 18th September 1926 passed a decree for Rs. 1,50,818 against the assesseees and in favour of the plaintiff in the case, that is, the Baneli Raj charging a portion of the property purchased in auction by the assesseees with the payment of this sum. It will be seen that this order was passed after the close of the financial year on the income of which assessment has been made in this case and that, when confirmation of the sale took place, this suit was pending.

8. In 1923 Kumar Ghananand, a minor son of one of the defendants in the above two mortgage suits who had not been made a party to them filed a suit in the court of the Subordinate Judge of Bhagalpur claiming, one-eighth share in the mortgaged property and praying that the sale be not confirmed in respect of this one-eighth share. As this suit was still pending when confirmation of the sale was due, it was directed by the High Court that assesseees should deposit security to the value of Rs. 3,20,633 being one-eighth of the purchase price of the property under both decrees and a deposit of this amount was accordingly made by the assesseees. By a judgment of the Subordinate Judge dated 15-9-27, it has been held that Kumar Ghananand's share and interest in the Srinagar estate did not pass to the assesseees by the sale and assesseees have now brought another mortgage suit against Kumar Ghananand in the Court of the Subordinate Judge of Monghyr, praying for a decree against Kumar Ghananand in respect of this one-eighth share of the property.

9. Having set out the facts of the case above, so far as is necessary, I now state the questions of law which the assesseees claim arise out of these facts.

10. The 1st question runs as follows: "When a bond is discharged and extinguished by a fresh bond and where the assesseees have credited the principal and interest of this bond in their books of accounts, can notional interest on the first bond be said to arise in years subsequent to the execution of the 2nd bond and can it be charged to income-tax subsequently?" It will be remembered that assesseees had in the year 1894 lent a sum of two lakhs to Kumar Nityanand and that in the year 1904, Rs. 2,33,000 and odd had accrued as interest on that bond, that in the later year assesseees gave back this old bond and had executed in their favour a fresh bond by the successors of Kumar Nityanand for a sum of Rs. 7,33,000 and odd, this being the total of 2 lakhs originally advanced, the interest accrued to date and 3 lakhs in cash advanced at the time the fresh bond was executed. Assesseees contend that they should have been taxed on that sum of Rs. 2,33,000 as the income of the year 1904-05 and all that they can be taxed on now is the interest, if any, notionally received on the fresh bond of 1904. The view of the assesseees would ordinarily be correct but the circumstances of this case are exceptional. In the first place, this sum of Rs. 2,33,000 and odd is not shown separately as interest realised in the assesseees' books of account of that year either in the interest account or in the personal account of the debtor. Secondly, when an attempt was made by the Income-tax authorities to assess them on that sum in the following year, they contested the point successfully either before the Collector of the District or the Commissioner of the Division. As the assessment records of that year have been destroyed it is difficult to get any documentary evidence on the point, but I have examined under section 37 of the Income-tax Act the clerk of the Income-tax Office, Monghyr, of the time who has since retired and also Rai Bahadur Chuni Lal Roy, at present Deputy Commissioner of Excise, who was Income-tax Dy. Collector in Monghyr from the middle of 1906 to the middle of 1908. According to the clerk, it was the Collector who directed that the predecessor in interest of the assesseees should not at that time be assessed on the amount of interest included in the renewed bond but that the amount will be assessed when it is actually realised by the purchase of the mortgage property or by

payment in cash. According to the Rai Bahadur the Collector in making the assessment actually included this amount, but the Commissioner of the Division on appeal by the predecessor in interest of the assessee accepted the appellants' contention and held that the amount should not be taxed in that year but should be taxed when the property subsequently passed to the assessee. I prefer to accept the evidence of the Rai Bahadur who is a witness of superior education and a trained intellect and assessee has done nothing to rebut the conclusion arrived at from this evidence. They have not even filed an affidavit challenging the correctness of the statements made by the witness. Assessee's counsel has filed a petition before me on the date the Rai Bahadur was examined claiming that I could not examine a witness under Sec. 37 when hearing an application under Sec. 66(2) and when I pointed out that I was also dealing with the case under Sec. 33 on assessee's own representation, he filed another petition withdrawing the application under Sec. 33. As however, I can take action and indeed legally do take action under Sec. 33 on my own initiative, it is obvious that the petition withdrawing the application originally filed under Sec. 33 does not remove that jurisdiction and that I can therefore examine witnesses under Sec. 37.

11. In my view therefore assessee cannot have it both ways and in view of the line of action taken by them in 1905, they can now be taxed on the interest accrued from the date of the original bond and subsequently received as the result of the sale and buying in of the judgment-debtors' property.

12. The 2nd question may be formulated as follows: "When a property is purchased in execution of a mortgage decree by the mortgagee subject to deposit of security sufficient to safeguard the interest of a party claiming a one-eighth share in the property to be unaffected by the decree, can the value of the whole property be taken into account for the purpose of computing profits, or, on the other hand, can the amount deposited in the court as security in these circumstances be claimed as deductible expenditure in computing profits"?

13. In my view these questions should be answered in favour of the Department. Assessee carry on a business in money-lending and are assessed on their income from that source under Sec. 10 of the Act. They can claim under Sec. 10(2) (ix) any expenditure incurred solely for the purpose of earning the profits or gains on which they are taxed. Assessee keep their accounts on the cash basis and the deposit made was certainly not an expenditure within the meaning of that sub-section. If assessee win the point at issue as against the 3rd party, they get back their deposit with interest, while, if they lose, they may forfeit their deposit. As a matter of fact, a judgment adverse to the assessee was given in this case in September 1927, that is, in a year subsequent to the year on the income of which they are being assessed, and the deposit may possibly become an expenditure of that subsequent year and may be deducted from their profits of that year accordingly, but it cannot be held to be an expenditure of the year on the income of which tax is now being assessed.

14. The 3rd question is formulated as follows: "Can assessee claim as admissible deduction from their income of that year the amount of decree obtained against them by a subsequent mortgagee who has subsequently been held by the courts to hold a prior mortgage over the property and is the sum which eventually turns out to be a charge on the property purchased by the assessee in a mortgage decree (which sum had not been considered by the assessee to be such charge on account of express covenant embodied in an original mortgage bond), an allowable deduction from taxable income in this case"?

15. This refers to the sum of Rs. 1,50,000 and odd which the courts held to be the value of the incumbrance held by the Beneli Raj on part of the property purchased by the appellants at auction sale. The facts in this matter are set out in paragraph 7 of the statement of the case and the court's finding adverse to the assesseees in this case was passed on the 18th September 1926, that is, in the year subsequent to the year on the income of which tax is being charged. This sum is in my view therefore not an admissible deduction from the income of the year on which tax is now being assessed under any of the sub-sections of section 10 of the Act. It may be a capital loss of the subsequent year or, on the other hand, it may be an admissible deduction from the income of that subsequent year in which the amount was actually paid to the plaintiff in the case.

16. The 4th question runs as follows: "When there is a covenant in a mortgage deed to capitalise interest in default of payment, can income-tax be charged in respect of the defaulted sums as interest when the mortgage property is subsequently sold in satisfaction of a decree for interest and principal"? In the bond of 1904, there was a stipulation that interest will be calculated half yearly and added to principal, or, in other words, compound interest was charged on the amount advanced. Assesseees in this case keep their accounts on a cash basis. They did not in the intervening years between the date of execution of the bond and sale of the judgment debtor's property receive payment of interest in cash or by constructive receipt in any way and the finding of the Madras High Court in the case *Pydah Venkatachalapathy Garu v. The Commissioner of Income-tax, Madras*(1) supports the departmental view.

17. The 5th question is formulated as follows: "Does the law contemplate taxation of notional receipts of income and profits arising from the purchase by the mortgagee of the mortgaged property? Is not a purchase by the mortgagee of the mortgaged property sold in execution of a decree a capital transaction"? In my view these questions should be answered in favour of the Department. The law nowhere defines 'income, profits or gains' and in heading 8 of the statement of total income called for under Sec. 22(2) of the Act and set out under statutory rule 19, I find that one of the sources of income is interest on mortgages. Clearly therefore the authorities who framed the statutory rule were of opinion that interest on mortgages was taxable. Assesseees' argument appears to be that when they purchase mortgaged property at auction sale this operation is a capital transaction and what they acquire is capital, but no authority has been advanced in support of this view and it is in my opinion unsound. The argument apparently is that when a creditor advances money on mortgage he acquires a contingent interest in the property mortgaged and when he subsequently buys in the property at auction sale he acquires the complete interest of the debtor in the property and this is a capital transaction. If it is true that the creditor acquired a contingent interest in the property at the time the mortgage was executed, this interest is acquired for the purpose of securing the debt and for no other purpose. It is not arguable that a debt can be satisfied only by the transfer of money or cash. It can be satisfied by receipt of money's worth and when the property finally passes to the creditor this passing of the property should be held to have satisfied the debt up to the value of the property which has passed. When a decree holder buys in mortgaged property, though the transaction is nominally a single transaction, it is in reality of a dual nature and what really happens is that the amount for which he buys in the property has been notionally received by him and with that notional receipt he purchases the pro-

perty. It is submitted therefore that this question should be answered in favour of the Department.

18. The 6th question is formulated as follows: "If the profits or gains arising to the assesseees from the buying of mortgaged property are taxable, what is the date on which the profits are to be deemed to have arisen? Is it the date of decree, the date of sale, the date of confirmation of sale, or the date of delivery of possession?"

19. In this case the decrees were passed on 22-12-17, Court sales took place on 19-11-24 and 31-1-25 and confirmation of sale on 18-12-25 and 21-12-25, while delivery of possession was effected on 30-9-26. The Income-tax Officer has held that the profits arose on the date of confirmation of sale and in this view I concur. Obviously, the profits did not arise or rather were not received by the assesseees on the date of the passing of the decree; for a decree is simply a finding of the court that a certain sum is due by the defendant to the plaintiff as interest, principal and costs. Again, the date of sale cannot be held to be the date on which the debt was extinguished, for the sale when first made is only provisional and contingent and becomes final only on confirmation. It is true that under section 65 of the Civil Procedure Code when a sale has been confirmed, the property shall be deemed to have vested in the purchaser from the time when the property is sold and not from the time when the sale becomes absolute. This action however gives only retrospective effect to the right in the property purchased but that right is created only after the sale is confirmed. Assesseees claimed before the Income-tax Officer that the interest on these mortgages, if received at all, was received at the time the delivery of possession was effected, that is, in the subsequent year. Clearly they cannot then raise the contention before the appellate authorities or before me that the profits were earned in the year in which the decrees were passed, for according to their own system of accounts and their own argument, the interest was realised only at the time of delivery of possession. I do not accept the view that the profits in this transaction were realised when delivery of possession was effected, for delivery of possession is only a symbolic act and right, title and interest had already passed to the assesseees the moment the sale was confirmed.

20. The 7th question runs as follows: "Assuming that there are profits arising out of this transaction which are legally taxable, are the assesseees entitled to deduct from these taxable profits expenses which are always entailed in taking delivery of possession and effecting mutation in the Collectorate registers?" In my view they are not, as title in the property passed to the assesseees at the time of confirmation of sale and these expenses were incurred subsequently and incurred not for the purpose of earning the profits now taxed but for the purpose of maintaining the title which had already passed to them or deriving benefit from the property which had already passed in satisfaction of the principal and interest.

21. The last question framed under Sec. 66 (2) is as follows: "What is the correct method of computing the value of the property acquired by the assesseees in this case? Is the bid of the assesseees to be assumed to be the correct valuation, or on the other hand, the valuation put on the property by the Civil Court Commissioners before the sales"?

22. The total amount on the basis of the two decrees due to the assesseees is Rs. 27,13,379. The Civil Court Commissioners had valued the property before the sale at Rs. 17,13,701 and the appellants bought in the property for Rs. 25,65,100. The method adopted by the Civil Court Commissioners for arriving at this valuation was follows: They took the gross income of each village, deducted land revenue, cesses and 10 per cent. as cost of collection and multiplied

the balance by 16. In other words, they took the value of the property as being 16 times its assumed annual net value. This method, however, is obviously a rule of thumb method and it must be presumed that the price bid for the property by the decree-holder is in the absence of proof to the contrary not an excessive price. Assesseees contend that for the purpose of putting a stop to later objections to the sale on the ground of inadequate price they bid much higher than the valuation made by the Court and that it was immaterial to the assesseees how high they bid so long as the sum bid was less than the decretal amount, because the judgment debtor had no other property from which the balance could be recovered. This argument is not convincing. Copy of the bid-sheet of the court has not been produced and it is impossible to say how the bidding proceeded. If the assesseees thought that the property was worth only 17 lakhs, that is, the Civil Court Commissioner's valuation, they would willingly have let the property go at the bid previous to their own final bid which must have been much higher than the Commissioner's valuation, for then they would have realised so much more of their dues. There is nothing on record to show that assesseees made an excessively high bid for the property and there is no good reason for their doing so. In my opinion, therefore, this question should be answered in favour of the Department.

23. I now submit a question of law arising out of this case for the decision of their Lordships under Sec. 66(1) of the Income-tax Act. The facts out of which this question arises are these: The total of the decrees passed in favour of the assesseees including principal, interest and costs upto the date of sale was Rs. 27,13,379 and the appellants bought in the mortgaged property for Rs. 25,65,100. The Income-tax Officer was of opinion that realisations should first be appropriated to interest and not principal and made assessment accordingly, while the Assistant Commissioner held that the appellants by making a declaration declaring what portion of the amount realised was interest and what portion was principal had made an appropriation in this case and he accordingly reduced the amount of tax assessed by the sum of Rs. 1,48,270, that is, the difference between the total amount of the decrees and the sum for which the property was bought in, holding apparently that this sum should be treated as representing interest and not capital. I do not find on record any declaration as referred to by the Assistant Commissioner and I do not understand what he meant by this declaration. The question which arises in this matter may be formulated as follows: "When a creditor executes a mortgage decree against a debtor and puts to sale the mortgaged property in satisfaction of the decree, if the total sum realised by the sale is less than the total of principal, interest and costs due, is the amount realized to be taken, for income-tax purposes, as credited after satisfaction of costs, first towards the payment of interest up to the amount of interest due and the balance only credited towards the satisfaction of principal, or, on the other hand, should the profit for income-tax purposes be taken as what is left over after satisfaction of principal and costs"?

24. I state my own opinion in this case as required by Sec. 66, subsection 1 of the Act. In my opinion the view taken by the Assistant Commissioner is incorrect. It has been held in the Privy Council case of *Venkata-dari Appa Rao v. Parthasarathy Appa Rao*(1) that as between creditor and debtor the ordinary rule as to payments by the debtor unappropriated either to principal or interest is that they are first to be applied to the discharge of interest. Further it is directed in Order 34 rule 13 of the Civil Procedure Code that the proceeds of a sale in satisfaction of a mortgage shall be brought into Court and applied as follows: Firstly, in payment of expenses of sale, secondly in payment of dues to a prior mortgagee, thirdly, in payment of all

interest due on account of the mortgage in consequence whereof the sale was directed and of the costs of the suit in which the decree directing the sale was made, fourthly, in payment of principal and lastly the residue, if any, shall be paid to the person whose property was sold. Again I find in Ghosh's Law of mortgage in India, 4th edition, Volume I at page 512 that if no appropriation is made either by the debtor or the creditor the latter will appropriate the payments as between principal and interest to interest in the first place and then to principal. I see no reason why the ordinary rule of appropriation as between creditor and debtor should not apply when arriving at profits or income for income-tax purposes and in my view after deduction of the costs which clearly were incurred in earning the profits, the balance should be credited in the first place towards the satisfaction of interest and only any sum left over after satisfaction of interest should be credited towards repayment of capital. At the same time, as the Department in this particular case has admitted that the assessee has a business in money lending the balance of principal which cannot be recovered should be allowed as a deduction from the assessed profits in the year in which such balance is definitely proved to be irrecoverable under the executive instructions contained in para 38 of the Income-tax Manual. This may be in the year in which this particular assessment was made or in a subsequent year.

K. P. Jayaswal, A. K. Mitter and P. B. Sinha, for the Assesseees.

The Advocate-General of Bengal, and C. M. Agarwala, for the Crown.

JUDGMENT

DAS, J.:—The Income-tax Officer assessed Raja Raghunandan Prasad Singh and Raja Deokinandan Prasad Singh, (who will be referred to as the assesseees throughout this judgment), for income-tax in respect of the year 1926-1927 upon the sum of Rs. 17,02,321 of which Rs. 16,23,459 in the judgment of the Income-tax Officer, represented the profits received by the assesseees in the previous year as the result of certain mortgage transactions with the proprietors of the Srinagar Raj. On appeal, the Assistant Commissioner reduced the assessed income to Rs. 15,53,033. At the request of the assesseees the Commissioner of Income-tax has stated a case to this Court under section 66(2) of the Income-tax Act 1922; and he has also referred a question of law, on his own motion, for our decision under section 66(1).

In order to appreciate the arguments which have been advanced before us, it is necessary to set out the facts as found by the learned Commissioner. Srinandan Singh, the proprietor of the Srinagar Raj, had three sons, Nityanand Singh, Kamlanand Singh and Kalikanand Singh. Sometime in 1892 Nityanand Singh separated from his brothers. In 1894 he borrowed Rs. 2,00,000 from the predecessors in title of the assesseees and executed a mortgage bond in his favour. In 1897 he borrowed Rs. 3,50,000 from the Banali Raj on the security of the properties belonging to him. The Banali Raj sued to enforce the mortgage and, on the 11th March 1902, obtained a decree for Rs. 4,57,189 against Nityanand Singh. On the 12th September 1903 Kamlanand Singh and Kalikanand Singh purchased from the Banali Raj the decree obtained by it as against Nityanand for the sum of Rs. 5,00,000, but being unable to find the money, executed a mortgage bond in favour of the Banali Raj. On the 20th October 1903 Kamlanand and Kalikanand purchased from Nityanand his share in the properties constituting the Srinagar Raj and became liable to satisfy the claims of the predecessor in title of the assesseees. The position on the 18th July 1904, which is a very material date in these proceedings, was as follows: Kamlanand and Kalikanand owed the assesseees

or their predecessor in title the sum of Rs. 4,33,135 on the transaction of 1894. They also owed the Baneli Raj Rs. 5,25,815 on the transaction of the 12th September 1903. It appears that the Baneli Raj was pressing for repayment. On the 18th July 1904 Kamlanand and Kalikanand paid Rs. 815 to the Baneli Raj. They borrowed another sum of Rs. 3,00,000 from the assesseees and paid the whole of it to the Baneli Raj in reduction of their indebtedness to the latter. They were still liable to the Baneli Raj for Rs. 2,25,000 for which they executed a fresh bond in its favour. Having borrowed the sum of Rs. 3,00,000 from the assesseees they executed a bond in their favour for Rs. 7,33,135 which included the sum of Rs. 4,33,135 which they owed the assesseees at the date of this fresh transaction. On the 7th November 1912 Kamlanand and Kalikanand borrowed another sum of Rs. 3,00,000 from the assesseees and paid the whole of it to the Baneli Raj in reduction of their indebtedness to it. It will appear then that the assesseees or their predecessor in interest advanced to Kalikanand and Kamlanand or their predecessor in title the sum of Rs. 2,00,000 in 1894, Rs. 3,00,000 on the 18th July 1904 and Rs. 3,00,000 on the 7th November 1912.

The assesseees instituted two suits on the two mortgages, one dated the 18th July 1904 and the other dated the 7th November 1912, and in due course obtained mortgage decrees as against the Srinagar Raj family. The mortgaged properties were put up for sale on the 19th November 1924 and the 31st January 1925; and they were purchased by the assesseees themselves. They obtained sale certificates on the 18th December 1925 and the 21st December 1925; and it appears that they obtained delivery of possession on the 30th September 1926. I may mention that the claim of the assesseees at the date of the sale on the mortgages to which I have already referred amounted to Rs. 27,13,379. The properties were however sold for Rs. 25,65,100. The Assistant Commissioner took the view that the sum of Rs. 25,65,100 after deducting thereout the cost, charges and expenses incurred by the assesseees up to the dates of the execution sales less the capital sums advanced represented the assessable income of the assesseees on the Srinagar mortgage transactions. The question which we have to consider is whether the view taken by the learned Assistant Commissioner is well-founded.

It was contended by Mr. Jayaswal on behalf of the assesseees that it is too late now to assess the interest on the Srinagar Raj mortgages to income-tax and that such interest should have been assessed, if at all, as it accrued due. Section 4 of the Income-tax Act which is the charging section provides that the Income-tax Act "shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing, or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise, or be received in British India." Mr. Jayaswal contends that the interests on what have been described as the Srinagar Raj mortgages as "income, profits or gains" accrued to the assesseees as they fell due from 1894 and that the claim of the Crown to assess that interest in the financial year 1926-27 is wholly inadmissible. Now in dealing with this point we are conclusively bound by the finding of the Commissioner that the assesseees kept their accounts on the cash basis and that those accounts do not show actual realisation of interest at any time. I think the fallacy of the argument lies in confusing a debt due but not realised with income. It is one thing to say that a claim accrued to the assesseees to recover the interest due to them by suit; it is another and a different thing to say that an income accrued to them.

But in truth the question has been settled by an authoritative decision of the Judicial Committee in *St. Lucia Usines and Estates Company Ltd., v.*

Colonial Treasurer of St. Lucia(1). I take the facts of that case from the head-notes, and they are these. In 1920 the appellants sold all their properties in St. Lucia and ceased to reside or carry on business there. In 1921 interest upon the unpaid part of the purchase price was payable to them, but it was not paid. The appellants were liable to pay income-tax for the year 1921 under the Income-tax Ordinance 1910, of St. Lucia only if the interest above-mentioned was 'income arising or accruing' to them in 1921. The question which their Lordships of the Judicial Committee had to try was whether the interest which was not paid in 1921 was nevertheless 'income arising or accruing' in 1921; and their Lordships had no difficulty in answering the question in the negative. In so deciding Lord Wrenbury who delivered the judgment of the Board said as follows:—"The words 'arising or accruing' occur repeatedly in the Ordinance, e.g., in Sec. 4, sub-sec. 1(a), (b), (c), (d) and (e), coupled with the words, 'and derived from' or 'or derived from'. Sometimes the expression 'derived from' is used alone, Sec. 5, sub-sec. 1 (a), (c), (g), (i) and (ii). The respondent contends that the above interest 'accrued' to the company in the year 1921, because it was payable in that year and none the less because it was not paid in that year. Their Lordships do not agree. The words 'income arising or accruing' are not equivalent to the words 'debts arising or accruing'. To give them that meaning is to ignore the word 'income'. The words mean 'money arising or accruing by way of income'. There must be a coming in to satisfy the word 'income'. This is a sense which is assisted or confirmed by the word 'received' in the proviso at the end of Sec. 4 sub-sec. 1". The words in the Indian Statute are exactly the same as those which Lord Wrenbury was considering in the case just cited. It seems to me that these words must receive the same interpretation in India as they did in the Colonial case. In my view the argument advanced by Mr. Jayaswal must be overruled.

It was next contended that by the express agreement between the parties the interest as it accrued due was added to the capital and that the agreement in fact effected capitalisation in the sense that no tax can be levied on it. All that we know from the case as stated by the Commissioner is that there were provisions as to compound interest in the bonds executed by the proprietors of Srinagar Raj. The question then resolves into this: Does the interest cease to be an income, profit, or gain, because at the end of certain specified periods it is added to the capital so that it may bear interest? I think not; and I am supported in my view by the decisions of the English Courts to the effect that an agreement as to compound interest does not effect capitalisation. The question was debated in *In re. Craven's Mortgage-Davies v. Craven*(2). The facts were these. By a mortgage of June 1, 1888, the mortgagor covenanted that on his death or on his son's death, whichever event should first happen, he, his executors, administrators, or assigns, would pay to the mortgagee the principal sum secured, together with simple interest thereon at the rate of 5 per cent per annum reckoned from August 10, 1887 up to the time of such death; and if the aggregate amount of this sum and interest or any part thereof should not then be paid, would pay interest on the unpaid part by equal half-yearly payments. The mortgagor predeceased his son and died in 1906. His executor paid to the mortgagee interest on the aggregate sum, consisting of principal and interest found due at the mortgagor's death. He now proposed to pay off the aggregate amount due on the mortgage, and claimed the right, in doing so, to deduct income-tax on so much of the aggregate sum as represented interest. It was argued that by the terms of the mortgage there was a contract that interest should be capital and that there-

(1) (1924) A. C. 508.

(2) (1907) 2 Ch. 448.

fore the executor was not entitled to deduct income-tax on so much of the aggregate sum as represented interest as income-tax was not payable on it. The argument was negatived by Warrington J. (as he then was) in these words: "Then there is one word I have to say on the question of capitalisation. It was argued that even if the interest before the death of W. G. Craven was within Sec. 40, it then ceased to be so, and became capital and itself liable to pay interest; in other words, that there was a contract that it should be capital. I do not think so. I find nothing in that deed to capitalise the interest or to change the character of the interest and make it something which it was not before. In order to recover this interest the executors of the mortgagee would have to sue the mortgagor's executor on the covenant for payment of interest. The effect of the last clause of the covenant is only that if the principal and interest is not paid at the right time, the unpaid interest is itself to bear interest. There is no capitalization."

The decision in this case was followed in *In re. Morris Mayhew v. Halton*(1) which was affirmed by the Court of Appeal in *Mayhew v. Halton*(2). It was pointed out by P. O. Lawrence, J. that "the decision in *In re. Craven's Mortgage*(3) has stood unchallenged for more than 13 years, and has in all probability been acted upon in numerous cases". In these circumstances the learned judge thought that he was relieved from having to form any conclusion of his own as his clear duty was to follow that decision which he accordingly did. In the Court of Appeal, however, there was an elaborate discussion; but the Court in the end, came to the unhesitating conclusion that an agreement as to compound interest does not effect capitalisation. In my judgment the view taken by the learned Commissioner is right; and I have no hesitation whatever in endorsing it.

It was then contended that the interest which accrued on the bond of 1894 is no longer assessable since that bond was extinguished so far back as the 18th July 1904. I have already mentioned that the proprietors of the Srinagar Raj owed the assesseees Rs. 4,33,135 on the transaction of 1894. They took a further loan of Rs. 3,00,000 from the assesseees on the 18th July 1904 and executed a bond in favour of the assesseees for Rs. 7,33,135. It is claimed that the transaction of the 18th July 1904 must be looked as if the mortgage bond of 1894 was completely paid off and that a fresh advance of Rs. 7,33,135 was made on the 18th July 1904. Mr. Jayaswal contends that the assesseees should have been taxed on the sum of Rs. 2,33,135 which represented the accumulated interest on the bond of 1894 as the income of the year 1904-05; and that it is too late now for the Crown to claim income-tax on that sum since it must be regarded as having been actually received by the assesseees in 1904. The answer to the argument is that, as the Commissioner has found, the assesseees keep their accounts on the cash basis and that as the Commissioner has also found, "this sum of Rs. 2,33,000 and odd is not shown separately as interest realised in the assesseees' books of account of that year either in the interest account, or in the personal account of the debtor". The inference is irresistible that the bond of 1894 was not extinguished from the point of view of the income-tax administration since nothing was received by the assesseees as income, profit or gain in that year. The view taken by the learned Commissioner is obviously right and must be affirmed.

The next question argued is formulated as follows in the case as stated by the Commissioner: "When a property is purchased in execution of a mortgage decree by the mortgagee subject to deposit of security sufficient to safeguard the interest of a party claiming a one-eighth share in the property to be unaffected by the decree, can the value of the whole property be taken into ac-

(1) (1921) 1 Ch. 172.

(3) (1907) 2 Ch. 448.

(2) (1922) 1 Ch. 126.

count for the purpose of computing profits, or, on the other hand, can the amount deposited in the court as security in these circumstances be claimed as deductible expenditure in computing profits"? The point arises in this way. In 1923 Kumar Ghananand Singh, one of the sons of Kalikanand Singh, filed a suit in the court of the Subordinate Judge of Bhagalpur claiming $\frac{1}{8}$ th share in the mortgaged property and praying that the sale be not confirmed in respect of his $\frac{1}{8}$ th share. It appears that in the mortgage suits which the assesseees instituted against the proprietors of Srinagar Raj, Kumar Ghananand Singh was by a mistake left out; and it was this circumstance which encouraged Kumar Ghananand Singh to claim, that the sale had not the effect of passing his $\frac{1}{8}$ th share in the mortgaged properties. As the suit was still pending when the assesseees applied for confirmation of sale, it was directed by the High Court that the assesseees should deposit security to the value of Rs. 3,20,633, being $\frac{1}{8}$ th of the purchase price of the property under the mortgage decrees; and it appears that the assesseees did furnish security for that amount. It is now contended that the profits or gains in the case should have been computed after making allowance for Rs. 3,20,633 as "an expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains." In my opinion it is impossible to give effect to the contention. It is sufficient to say that the assesseees have not incurred any expenditure at all though they have given security for a definite sum and that if they incurred any expenditure it was not incurred solely or otherwise for the purpose of earning such profits or gains. It may be that if Kumar Ghananand Singh ultimately succeeds in his action, the assesseees will incur a loss; but the Income-tax Department will no doubt take such loss into consideration if and when it takes place and set it off against the income, profits or gains under any other head under section 24 (1) of the Income-tax Act. The question in my view does not arise in the present proceeding; and I must accept the view which has been taken by the learned Commissioner on this point.

The next point arises with reference to a decree which Baneli Raj has obtained against the assesseees. In enumerating the mortgage transactions of the Srinagar Raj I have omitted to mention that on the 29th April 1916 the proprietors of that Raj executed a mortgage bond in favour of the Baneli Raj to secure an advance of Rs. 7,00,000. The Baneli Raj brought a suit in 1923 to enforce the mortgage bond of the 29th April 1922 and in the course of that suit a question of priority arose as between the Baneli Raj and the assesseees. On the 18th September 1926 the Court decided against the assesseees, and gave a decree to the Baneli Raj, the effect of which is that that Raj is entitled to recover Rs. 1,50,000 from the properties which have been purchased by the assesseees. In these circumstances the assesseees claim as admissible deduction from their income the amount of the decree obtained against them by the Baneli Raj. The answer to the argument is that no expenditure has yet been incurred by the assesseees and it cannot be allowed at the present moment. It appears that the decision of the learned Subordinate Judge was pronounced on the 18th September 1926, i.e., in the year subsequent to the year on the income on which tax is being charged. It is obvious then that that sum cannot be admissible deduction from the income of the year on which tax is now being assessed under any of the sub-sections of section 10 of the Act. It may be a capital loss of the subsequent year, or it may be an admissible deduction from the income of the subsequent year in which the amount was actually paid by the assesseees to the Baneli Raj.

It was next contended that the law does not contemplate taxation of notional receipts of income and profits arising from the purchase by the assesseees of the mortgaged properties and that the transaction in respect of which tax has been assessed by the Crown was in fact a capital transaction and was therefore not

side the provisions of the Income-tax Act. I am unable to agree with the contention. The assesseees were entitled to recover from the Srinagar Raj money or money's worth. The properties which they have now purchased represent the money originally advanced to the Srinagar Raj together with the accumulated profits on the advances. It is in fact the money originally advanced with the accrued profits in another form. So the matter stands on principle; but it is also concluded by the decisions in *Scottish and Canadian General Investment Co., Ltd. v. Easson*(1) and *California Copper Syndicate v. Hurris*(2). In the former of the cases, the question arose in this way. The appellant held bonds of a company unable to meet the coupons for the interest thereon for the half year from 1st July 1915. A reorganisation involving the formation of a new company took place, and the appellant surrendered the bonds, with the unpaid coupons, and received in exchange 5 per cent bonds of the new company of equivalent face value, bearing interest from 1st July 1917, together with an issue of debentures of the new company equal in face value to 10 per cent. of the face value of the surrendered bonds, such debentures being thus equivalent in face value to the coupons for the two years' interest from July 1st, 1915 to July 1st 1917. It will be noticed that the interest was paid in kind, not in cash; and, in computing the profits of the appellant, a sum equal to 75 per cent of the face value of these debentures, as representing their actual value, at the time of receipt, was included as income received. This method of computation was contested by the assesseees; but it was held that, there being before the Commissioners evidence sufficient to enable them to determine that the debentures represented the two years' interest on coupons surrendered, the value of the debentures had been properly included in the computation of the company's profits, and that there was no material on which to question the Commissioners' finding that 75 per cent of the face value of the debentures represented the profit.

In the latter of the cases, a company formed for the purpose, *inter alia*, of acquiring and reselling mining property, first acquired and worked various mines, and then it resold the whole to a second company receiving payment, not in cash, but in fully paid shares of the latter company. The Income-tax department took the view that the difference between the purchase price and the value of the shares was a profit assessable to income-tax. It was contended on behalf of the company that the case was one of substitution of one kind of capital for another and that, in any case, no tax should be levied until the value of the shares had been realised in money. The Court negatived the contention and held that the view taken by the Income-tax department was correct. In delivering the judgment of the Court, Lord Trayner said as follows: "But it was said the profit was not realised profit, and therefore not taxable. I think the profit was realised.....No doubt here the price took the form of fully paid up shares in another company, but if there can be no realised profit except when that is paid in cash, the shares were realizable and could have been turned into cash." These cases appear to me to be relevant, and I must accept the conclusion reached by the Commissioner on this point.

The next point argued raised the question whether the Income-tax Department employed a correct method of computation. What fell to be decided was what was the profit made by the assesseees on the Srinagar mortgages. At the date of the sale there was due to the assesseees Rs. 27,13,379 on the mortgages in question. They purchased the properties at the court sale for Rs. 25,65,100. The assesseees contend that the real value of the properties was not Rs. 25,65,100, the price paid by them, but Rs. 17,13,701 as valued by the Civil Court Commissioner.

(1) 8 Tax Cas. 265.

(2) 5 Tax Cas. 167.

Now if Rs. 17,13,701 be regarded as the value of these properties, then it must follow that considerably less profit was made by the assesseees. I am not prepared to attach any importance to the valuation as made by the Civil Court Commissioner; but it is sufficient for me to say that the Income-tax Department did not err, in point of law, in taking the view that the price paid by the assesseees represented the true value of the properties and that there is no material in the record which would enable us to say that its conclusion in point of fact, is not a correct one.

The next question argued is one of considerable difficulty, and it is necessary for me to proceed with care. The question is formulated as follows in the case stated by the Commissioner; "if the profits or gains arising to the assesseees from the buying in of mortgaged property are taxable, what is the date on which the profits are to be deemed to have arisen? Is it the date of decree, the date of sale, the date of confirmation of sale, or the date of delivery of possession"? The importance of the question lies in the circumstance, that, in order to enable the Crown to claim income-tax in the case, it must be shown that the profits accrued, arose or were received by the assesseees in "the previous year", that is to say, in the year ending with the 31st March 1926.

The mortgage decrees were pronounced on the 22nd December 1917, so that, if that date be taken as the material date, it must follow that the Crown has lost its right to recover income-tax in respect of the profits made by the assesseees on the Srinagar mortgages. The argument that that date must be taken to be the material date was not seriously pressed before us, and it is not necessary for me to say more than this that the obtaining of decrees is not equivalent to realization of profits. An elaborate argument was however advanced to us in support of the view of the assesseees that the profits must have been received by them on the 19th November 1924 and the 31st January 1925, the dates of the court sales. If this argument be well-founded, then it must again follow that the present assessment must go, though the Crown has the right to proceed against the assesseees under section 34 in respect of the income which escaped assessment. We are informed that the Income-tax Officer has served notice on the assesseees under section 34; so that it must follow that the question argued before us is of no practical importance so far as this case is concerned. But the question is of general importance and it is necessary that we should decide it.

If I have understood Mr. Jayaswal's argument, it is this: it is quite an error to suppose (so he contends) that the immovable properties purchased by the assesseees represent the actual advances made by them together with the profits thereon. The true position according to him is that which has been put so clearly by the Commissioner in the case stated by him. "When a decree holder buys in mortgaged properties", so says the Commissioner in paragraph 17 of the case, "though the transaction is nominally a single transaction, it is in reality of a dual nature and what really happens is that the amount for which he buys in the property has been notionally received by him and with that notional receipt he purchases the property." Mr. Jayaswal contends that what must be regarded is, not the purchase of the properties by the assesseees, but the notional withdrawal of the purchase money by them. A third party might have purchased the properties and the assesseees would have been entitled to withdraw the purchase money from court in satisfaction of their claim as against the Srinagar Raj. The position is not different, according to the argument advanced before us, because the assesseees who are the decree holders have themselves bought in the properties. Mr. Jayaswal relies upon Order 21 Rule 72 of the Code which provides that where a decree holder purchases with the express permission of the court, the purchase money and the amount due on the decree may be set off against one another and the court executing the decree shall enter up satisfaction of the decree in whole or in part accordingly. Mr. Jayaswal contends that though the assesseees have not in

fact paid the purchase money into court and have therefore not withdrawn the purchase money, the transaction must be regarded as if they paid the purchase money and withdrew that purchase money, so that it must follow that the profits accrued to them at the dates of the sales.

As I have said the argument is a weighty one; but at the same time if this argument is to succeed, it must follow that the material dates are not the dates of the sales but the date on which the Court entered up satisfaction of the decree. Now there are no materials in the record to enable us to decide when the court in fact entered up satisfaction of the decree; and, this being the position we are not at liberty to question the Commissioner's finding on this point.

But in truth the question is of a more complicated nature. When a third party purchases properties at court sales, he is required to bring the money into court at once for the protection of the decree-holder. But where the decree holder himself purchases the property, he is not in need of the protection; and so the Code provides that the purchase money and the amount due on the decree may be set off against one another. But does it follow that, because the set off is allowed under the provisions of the Code, the profits are actually received when the Court enters up satisfaction of the decree? The solution of the question requires a consideration of some of the more important sections in the Code relating to court sales.

It is abundantly clear from section 65 of the Code that the property does not vest in the auction purchaser until the sale has become absolute. I do not overlook the actual words of section 65 which provides that the property shall be deemed to have vested in the purchaser from the time when the property is sold and not from the time when the sale becomes absolute. Section 65 creates a statutory fiction, but as that section makes it quite clear, the fiction comes into play when the sale has become absolute and not a moment sooner. The reason is obvious. A period of at least thirty days must expire from the date of sale before the sale can become absolute. During that period the sale is liable to be set aside at the instance of the judgment debtor on the ground of irregularity in publishing or conducting the sale under Order 21 Rule 90 of the Code, or on deposit by him in court of the amount specified in the sale proclamation together with a percentage on the purchase money by way of compensation to the purchaser under Order 21 Rule 89. It is also liable to be set aside under Order 21 Rule 91 at the instance of the auction purchaser on the ground that the judgment debtor had no saleable interest in the property sold. A judicial sale is therefore liable to be set aside; and it is for this reason that the Code provides in Rule 92 that where no application is made under Rule 89, Rule 90 or Rule 91 or where such application is made and disallowed the court shall make an order confirming the sale and thereupon the sale shall become absolute. Now let me turn to section 65 which provides that where immovable property is sold in execution of a decree and such sale has become absolute the property shall be deemed to have vested in the purchaser from the time when the property is sold and not from the time when the sale becomes absolute. This section has a long history behind it; but it is not necessary for me to deal with it except to point out that the emphasis is on the words "and such sale has become absolute". It is obvious therefore that the statutory fiction created by section 65 comes into play only when the sale has become absolute.

Now if this position be accepted, then it must follow that the entering up of satisfaction of the decree by the Court under Order 21 Rule 72 of the Code does not decide the question as to the point of time at which profits must be said to have accrued to the assesseees. Section 72 does not say when the Court shall enter up satisfaction of the decree if it allows the purchase money to be set off against the amount due on the decree. I apprehend that if the Court execut-

ing the decree knows its duty it will not enter up satisfaction of the decree until the sale has become absolute. I may turn to the provision of Order 21 Rule 93 of the Code on which reliance was placed by Mr. Jayaswal. That rule provides that where a sale of immovable property is set aside under Rule 92, the purchaser shall be entitled to an order for repayment of his purchase money, with or without interest, as the court may direct against any person to whom it has been paid. Mr. Jayaswal contends that this rule clearly contemplates that the decree-holder may be entitled to withdraw the purchase money from court if the property is purchased by a third person; and he argues that if in this case a third party had purchased the properties and the decree-holder had withdrawn the money from court it could not be urged that the profits did not accrue to the decree-holder at the date of such withdrawal. But Rule 93 itself provides that if the sale is set aside the purchaser shall be entitled to an order for repayment of his purchase money. A case of this nature is not before us, for properties have been purchased by the decree-holder and not by a third party. But I apprehend that the decree-holder would hardly deal with the money so withdrawn as his profit, so long as the sale was liable to be set aside. The question has been debated in England as to when a profit is actually earned. In *Commissioner of Taxes v. The Melbourne Trust, Limited*(1) their Lordships of the Judicial Committee said that a profit can be said to be earned when it is dealt with as a profit. They agreed that in ordinary cases this synchronises with the realisation of the sums that swell the assets of the person or company, but they pointed out that a person or a company is entitled to hold a part of their realisation in suspense so that such realisations can hardly be said to be profits so long as they are held in suspense. Assuming that in this case a third party had purchased the properties, and assuming that the assesseees were allowed to withdraw the purchase money, subject to the statutory liability to bring the money into court if the sale was set aside under Rule 92 of the Code, could it be said as a matter of law that the purchase money so withdrawn was a profit in the hands of the assesseees? I apprehend that the answer must be that it would be regarded as a profit if in fact it was dealt as such by the assesseees; but that it would not be a profit if it was not dealt as such by the assesseees. It would, in my judgment, be open to the assesseees to hold the money in suspense and to say to the Income-tax Officer, if any attempt was made to tax it, "We do not know our position with respect to this money until the sale has become absolute, for there is a statutory obligation on us to bring it into court, should the sale be set aside under Order 21 Rule 92 of the Code. Please call when the sale has become absolute; for until then we do not propose to deal with the money as in any way belonging to us." In my judgment such an answer would be conclusive to any attempt on the part of the Income-tax Officer to tax the money before confirmation of sale.

But as I have said we are not concerned with the question as to what the position would have been, had the properties been purchased by a third party. The only question before us is whether, the decree-holder having purchased the properties, it can be said that the profits accrued when the court entered up satisfaction of the decree. In my opinion the answer must be in the negative for the reason that such entering up of satisfaction of the decree is liable to be recalled if the sale is ultimately set aside. We were invited to consider the case of two merchants having claims against each other and we were asked whether it could not be said that incomes actually accrued to them, though nothing was in fact received by either of them if they set off their claims against each other. In my judgment such a case is not parallel to this. In the case of merchants, the set-off is final, absolute and decisive; but, in a case of this nature, it is conditional on the sale becoming absolute; and as I have said, no court know-

(1) (1914) A. C. 1001.

ing its duty would enter up satisfaction of the decree before the sale has become absolute.

But in truth I regard the transaction as something entirely different. The Srinagar Raj might have sold the properties to the assesseees in satisfaction of their liability to the latter. They did not voluntarily sell the property but in my judgment the involuntary sale stands exactly on the same footing as a voluntary sale. If this be so, then, the statutory fiction notwithstanding, it is impossible to say for the purpose of the Income-tax Act that the profits were realised by the assesseees at any time before the sale became absolute. I will apply one simple test. Could the assesseees apply for a delivery of the properties to them before the sale became absolute? Order 21 Rule 95 is clear on this point. That rule provides that "where the immoveable property sold is in the occupancy of the judgment-debtor, or of some person on his behalf or of some person claiming under a title created by the judgment-debtor subsequently to the attachment of such property and a certificate in respect thereof has been granted under Rule 94, the Court shall, on the application of the purchaser, order delivery to be made by putting such purchaser or any person whom he may appoint to receive delivery on his behalf in possession of the property, and, if need be, by removing any person who refuses to vacate the same". It is obvious that an application under Rule 95 cannot be made until a sale certificate has been granted to the decree-holder under Rule 94. How can it then be said that the profits accrued to the decree-holder at the date of the sale when they were not entitled to an order for delivery of possession of the properties to them? In my opinion the view taken on this point by the Commissioner is right and it ought to be affirmed.

I need not discuss the other question, namely, whether the critical date is the date of delivery of possession which was effected on the 30th September, 1926. It was not seriously contended that that is the material date to be regarded by us. In my view the profit was a realisable profit at the date when the sale became absolute.

The last question argued before us, namely, whether the assesseees are entitled to deduct from the profits expenses which are always entailed in taking delivery of possession and effecting mutation in the collectorate registers must be answered in favour of the view taken by the Commissioner. If I am right in taking the view that the profits must be said to have accrued to the assesseees at the date when the sales became absolute, then it must follow that the expenses incurred by the assesseees subsequent to that date must be entirely ignored.

The learned Commissioner has submitted a question for our consideration under section 66(1) of the Income-tax Act. The facts as stated by the learned Commissioner are these. The total of the decrees passed in favour of the assesseees including principal, interest and costs up to date of the sale was Rs. 27,13,379 and the assesseees bought in the mortgaged property for Rs. 25,65,100. The Income-tax Officer was of opinion that the realisations should first be appropriated to interest and not principal; and he made the assessment accordingly; but the Assistant Commissioner held that the assesseees by making a declaration declaring what portion of the amount realised was interest and what portion was principal has made an appropriation in this case and he accordingly reduced the amount of tax assessed by the sum of Rs. 1,48,279. The question which the Commissioner submits for our consideration is—"when a creditor executes a mortgage decree against a debtor and puts to sale the mortgaged property in satisfaction of the decree if the total sum realised by the sale is less than the total of principal, interest and costs due, is the amount realised to be taken, for income-tax purposes, as credited after satisfaction of costs, first towards the payment of interest up to the amount of interest due and the balance only credited towards the satisfac-

tion of principal, or, on the other hand, should the profit for income-tax purposes be taken as what is left over after satisfaction of principal and costs"? The view taken by the Commissioner is that the Income-tax Officer was right in holding that realisations should first be appropriated to interest up to the amount of interest due. In stating his own opinion he has relied upon the law of appropriation as propounded by their Lordships of the Judicial Committee in *Venkatadri Appa Rao v. Parthasarathi Appa Rao and others*(1) and on certain passages in Sir Rash Behari Ghosh's Law of Mortgages. In my opinion it is not necessary to get entangled in the law of appropriation since the position here is perfectly clear. The assessee advanced a sum of money to the Srinagar Raj. They have realised a certain sum of money from them. It is obvious that the profit which has accrued to the assessee is the sum of money realised by them less the capital sums advanced by them. The learned Advocate-General appearing on behalf of the Crown supports the view of the learned Commissioner. He contends that there is still a sum of money due to the assessee from the Srinagar Raj; and it may be that they will proceed to realise what is still due to them in subsequent years. Now the question put to us by the learned Commissioner arises on the facts as stated by him. We do not know whether it is possible for the assessee to recover anything more from the Srinagar Raj. We were not told whether the assessee have taken out execution against the Srinagar Raj to realise what is still due to them. In these circumstances and as there is no material in the record to enable us to decide the point, I am unable to say that the view taken by the Assistant Commissioner is erroneous.

As all the points raised on behalf of the assessee have failed, they must pay the costs of this reference: hearing fee Rs. 500.

KULWANT SAHAY, J.:—I entirely agree with. Das, J. and I have nothing further to add.

WORT, J.:—This is a case stated by the Commissioner of Income-tax on some nine questions of law. The facts have already been set out in the judgment of my learned brother and it is therefore unnecessary for me to state them. Taking the questions in the order in which they have been set out in the Court by the Commissioner, the first is whether notional interest on the first bond can be said to arise in years subsequent to the execution of the second bond and can it be charged to income-tax subsequently. The argument in this connection on behalf of the assessee sufficiently indicates the meaning of the first question and it is this, that the interest on the bond of 1894 arose or accrued yearly and that had the Income-tax Officer been so minded he could have charged the assessee income-tax on that interest from year to year whether in fact it was paid by the mortgagor to the mortgagee or not. As that has not been done the interest which had accrued from year to year was capitalised in the bond of 1904 and the right of the income-tax authorities to levy income-tax on that sum has been lost for ever. As we know the interest on 1904 bond, the interest on the 1912 bond was received by the assessee as a result of the decree which was obtained in the year 1917; in other words all the loans with interest thereon were ultimately obtained in a lump sum. Substantially the question is whether the income represented by this interest arose or accrued at such a date as to be assessable in the income-tax year for which the income-tax is sought to be charged in respect thereof, that is to say, the income-tax year of 1926 and 1927. This as we shall see, raises another question. The proceeds of the decree were obtained in the year 1924-25 or 1925-26 according to what view is taken of the point of law which arises in connection therewith. But that, as I have stated, raises another question which will be dealt with in a moment.

(1) I. L. R., 44 Mad. 570.

The section which is under consideration in this connection is section 4 which provides that "save as hereinafter provided, this Act shall apply to all income, profits, or gains, (as described or comprised in section 6) from whatever source derived, accruing, or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise or to be received in British India." It is said that this income from these mortgagors accrued or arose in the years in which the mortgagors became liable to pay interest and it is pointed out that the section to which I have made reference uses the words "to accrue, or accruing or arising or received" and it is said therefore that it is clear that the legislature used the expression 'accruing', not in the sense of the actual receipt of the income. This is to be gathered from that expression used in the section 'or received'. Quite apart from the construction of this section, it seems to me to be a very bold proposition to assert that a person might be charged for income-tax when he may have no income, and the learned Counsel on behalf of the assessors admits that he is driven back to the position in which he must agree that a person may be so charged although he has not received the sums which in fact go to make up his income. This question is not without authority. It is true that the decision which has been quoted, and which I refer to, is not binding on this Court, but it is, if I may be allowed to say so with great respect a very weighty decision on the very subject which is debated before us. It is a case of *St. Lucia Usines and Estates Company, Limited v. Colonial Treasurer of St. Lucia*(1). In that case a Company ceased to carry on their business and sold their assets in the year 1920. A part of the purchase price was left unpaid and was secured by, what is known locally, as 'vendor's privilege' with a covenant to pay in the following year (the 30th November) that sum so left together with interest at 6 per cent. from 19th November 1920. Interest was not paid and the Company obtained a judgment and was subsequently paid. The Company was held liable to pay income-tax on the proceeds of the judgment or a part thereof. Lord Wrenbury delivering the opinion of the Board stated that the income-tax was an annual tax on income derived from any source and is due and payable in respect of the year in which it is assessed, and that the section under the Income-tax Ordinance then under consideration was section 3 which enacts that every person receiving income or to whom income shall accrue shall in respect of such income pay an annual income-tax at certain defined rates. He points out that for the purpose of local income-tax law it is necessary either to show that the person sought to be charged was a person residing in the colony or a person not residing in the colony but having income derived from a source in the colony, and he points out that the question for determination was whether in the year 1921 the Company had income derived from a source in the colony; it should be remembered that they were held not to be residents in a colony in that year. It is pointed out that the respondent, that is the Colonial Treasurer of St. Lucia argued that the interest on the unpaid sum had accrued in the year 1921 and therefore the Company could be made liable. It is pointed out by Lord Wrenbury that the words "income arising or accruing" were not equivalent to the expression "debts arising or accruing" and there must be a 'coming in' to satisfy the word "income". As a result it was held that the Company were liable to be assessed in the year 1921. The matter under consideration in this case is, both so far as the word itself is concerned and the general proposition underlying the statute and the ordinance, the same. To repeat the words of Lord Wrenbury in order that this income by way of interest should have accrued there must be something to satisfy the word 'income', that is to say, there must be some 'coming in' to come within the provisions of the income-tax law. In my judgment it cannot be said that this income by way of interest not being paid accrued from year to year up to the year 1904.

(1) (1924) A.C. 508.

Now the other aspect of this question which has been argued is this. First so far as the bond of 1894 is concerned there was a provision for rests of four months, but as regards the bonds of 1904 and 1912 there was rests six monthly. It is argued as an alternative to the argument which I have dealt with in regard to the bond of 1894, interest not having been paid it was capitalised for four months that is, every four months interest then accrued due became capital and interest was to be paid thereon. It is said as a result of this that the payment received by the assessee from these three bonds is a capital accretion and not income within the meaning of the Act at all. I am not certain that this question in this argument really arises on the case stated by the Commissioner. But it does arise, I think, in another form with regard to the bond of 1904. This point has been dealt with by English authorities. I propose to follow them.

The first case is the case of *Craven's Mortgage: Davies v. Craven*(1). The mortgagor in that case covenanted that on his death or on the death of his son, whichever event should first happen, a certain sum of money would be paid to the mortgagee his executors, administrators or assigns, together with interest at the rate of 5 per cent per annum up to the time of such death and, if the aggregate amount of such sum and interest or any part thereof should not then be paid, then and in such case, ascertaining the aggregate, the part so remaining unpaid would be paid to the mortgagees, etc., etc., with interest on the aggregate sum or for the unpaid part thereof at the rate of 5 per cent. per annum by equal or half year payments. The interest at the date of his death was unpaid. The executor of the mortgagor then proposed to pay the mortgagee or his executors the principal and interest deducting income-tax therefrom. The argument on behalf of the mortgagees was that they were not entitled to deduct income-tax under section 40 of the Income-tax Act of 1853, because at the time when it was sought to deduct the income-tax, the amount had become capital sum and not income or to put it in the words of the argument, it was capital and could not be treated as "yearly rate of interest." It is true that the case rests on the construction of an English Act of Parliament; but the same question which we have to determine arose in that case. The major portion of the judgment, however, does not refer to this matter; it is the latter paragraph only in which Warrington, J., as he then was, refers to this question stating that it was argued that this interest became capitalised and that there being a contract to capitalise, it ceased to be interest and therefore income-tax was not deductible. He came to the conclusion that there was no capitalization and there was no agreement to that effect. He states: "I find nothing from that deed to capitalise the interest or to change the character of the interest and make it something which it was not before and that in order to recover this interest the executor of the mortgagee would have to sue the mortgagor's executor on the covenant for payment of interest". He then refers to the last part of the covenant under consideration to the effect that if the interest is not paid at the right time unpaid interest is itself to bear interest.

The next case is *In re. Morris: Mayhew v. Halton* (2). That was a covenant where a mortgagee was to pay compound interest at the rate of $4\frac{1}{2}$ per cent per annum with annual rests and the same questions which were decided before Warrington, J., came to be considered in this case. Lord Sterndale in delivering his judgment stated that the expression "yearly rests" added nothing to the matter, the contention in that case being that all that could be deducted was tax on the interest of the last year. It was contended that the words "compound interest", when rests are taken, turns the interest overdue into capital. Therefore when there was a payment to the mortgagee it was a repayment of a

(1) (1907) 2 Ch. 418.

(2) (1922) 1 Ch. 126.

capital. It was contended that the word "capitalisation" as used in many of the books in this connection was fallacious and Lord Sterndale points out that "when those sums of interest came to be paid at the end of the time when payment is made, although interest had been charged on them, and although, as a matter of book-keeping, they had from time to time been added to the capital, they did not cease to be interest." No further statement need be made with regard to the matter than what is stated in the judgment to which I have referred. In other words interest was interest whatever you may call it. If it was interest in its inception it remains interest whether you charge interest upon it or not. Now as to the question whether the fact that the consideration for the bond of 1904 was first of all the interest overdue on the bond of 1894 plus a cash payment then made and that the interest was to be charged thereon, had the result of capitalising the interest on the bond of 1894. This part of the argument more specifically deals with the matter which is put in the first question by the Commissioner, as I have already stated. He puts it in the form of question whether the interest on the bond of 1904 can be said to arise after the year 1904 under these circumstances. It seems to me that making the overdue interest on the bond of 1904 a part of the consideration for the bond of 1904 is nothing more than the condition relating to the bond of 1894 or 1904, that is, that interest being unpaid interest, interest should be charged thereon. It is argued of course that here is a definite contract to capitalise the sum and that the view which was expressed by Warrington, J., in the case of *Craven's Mortgage* was to the effect that if there had been a contract to capitalise the sum the question will be decided differently. Here we have all the essentials of actual turning this interest into capital and therefore the sum of Rs. 2,33,000 cannot be the amount upon which the income-tax authorities should charge income-tax. I do not agree with the argument advanced. The most that can be said with Warrington, J.'s judgment in this respect is that he definitely stated in that case that there was no contract to capitalise the interest. I cannot see myself that the transaction which was entered into in 1904 in any way alters the character of the sum of Rs. 2,33,000 which formed one of the liabilities of the mortgagor and was in the first place, at any rate, interest. In my judgment interest remains interest to the last and therefore the first question put to the Court by the Commissioner shall be answered in favour of the Crown.

The next question is that when the purchase by the mortgagee in execution of a mortgage decree subject to deposit of security sufficient to safeguard the interest of a party claiming one-eighth share in the property to be unaffected by the decree, can the sum be deducted as expenditure. I fail to see in any way that the assessee can have this privilege. As is pointed out in the case, a judgment adverse to the assessee was given in September 1927, that is, in a year subsequent to the year on the income of which they are being assessed. I agree with the view expressed by the Commissioner that it may be an expense for the year 1927; but as the matter is not finally disposed of it seems to be open to the Commissioner to decide that it is an expenditure which can be taken into account in a later assessment year.

The next question is whether a deduction can be made with regard to a sum of Rs. 1,50,000 which the Courts held to be the value of the encumbrance held by the Banali Raj being a prior encumbrance. The judgment in this case was given on the 18th September 1926 and the same answer which was given to the second question, it seems to me, applies to this.

The fourth question is answered by this judgment on the first and should be answered in favour of the income-tax authorities.

The fifth question is whether the transaction in which the mortgagee purchased the mortgaged property is a capital transaction or whether from that transaction it can be said that the mortgagee has recovered the income to which he was entitled by reason of the obligation of the mortgagee to pay him interest. In one sense of the word, of course, the transaction is a capital transaction; but the question is, can the mortgagee escape from paying the income-tax on sums of money which have been held to be interest and income therefrom and not capital by reason of the fact that he purchased, when the debt became due by the mortgagor to the mortgagee, the mortgaged property. The real question in this case is whether assuming that part of the debt which represents interest and upon which income-tax is assessable can, in any sense of the word, be said to have been recovered by the assessee. It appears to me that if the answer is in the affirmative it cannot be said that the income received ceased to be income, because he entered into capital transaction a part of the consideration for which the income was so received. That question, in my judgment, should also be answered in favour of the income-tax authorities.

The next question in substance is at what date can it be said that the assessee received the income by way of interest assessable in this case. It should be remembered, as I have indicated in discussing the earlier matters, that the mortgaged property was put up for sale in execution and that the mortgagee himself with the consent of the Court purchased it. He did not receive the money in cash in satisfaction of his judgment debt as he would have done had a third party purchased it. It is contended first of all by the Counsel on behalf of the assessee that the sum received in this manner was received on the date of the sale which was in December 1905. The contention on behalf of the Crown, however, is that the sums so received were not received on that date but it was received notionally on the date on which the sale was confirmed. The reason for raising this question appears to be this, that if this was received on the date of the sale then it was received a year before the year, that is to say, April 1925 to April 1926, which is to be taken for the purpose of assessing the income for the assessment in question, that is to say, the income-tax year 1926-27. If, however, it was received notionally on the date of the confirmation of the sale it will bring it within, what I may call, the computing year 1925-26.

This point was argued as a question of law; but I have the gravest doubt whether it was a question of law at all. Mr. Jayaswal on behalf of the assessee, as I have already indicated, argues that in fact that which was chargeable to income-tax in this case was received notionally when the sale took place in December, that is to say, took the form of the judgment-creditor being allowed to exchange his decree or part thereof for the mortgaged property. The reason why I do not think it was a question of law is this: we are not considering when the assessee as purchaser became, if I might use the expression, "absolutely" entitled to the property or when, to repeat myself in other language, the assessee was allowed to use his decree as if it represented cash and in payment for the mortgaged property. It is uncertain whether satisfaction was entered on the date of the sale or shortly after or not or was paid on the date on which the sale was confirmed. In my judgment, however, these are irrelevant matters. It was pointed out in this connection by the Crown that the transaction was not complete in two ways; first, it had not been confirmed and secondly as a result thereof the whole transaction might hereafter be set aside. However, I do not see any difference in this case from the case of an ordinary commercial transaction which is not represented by the passing of cash or its equivalent but which on a book-keeping entry shows a profit. As I have said, this appears to me to be not a question of law but essentially a practical one; in other words it was open to the income-tax authorities to say to the assessee "you have entered into a transaction which shows a profit; that profit in your case is income and is therefore taxable: if subsequently it is shown that it is a bad debt you will be entitled to an allowance for it hereafter". What the Crown has done in this case, however, is to say (it is true for their own

The assessee, a limited company, in 1922 took a lease inter alia of certain house property which was subject to a building lease for 50 years granted by the owners in 1920 in favour of the Tata Industrial Bank Ltd. containing a forfeiture clause in case of the lessees (Bank) going into liquidation. In 1923 on the Tata Industrial Bank Ltd. entering into voluntary liquidation to effect an amalgamation with the Central Bank of India Ltd. the assessee claimed to determine the lease, whereupon the claim was compromised by the Central Bank of India Ltd. in consideration of a lump sum payment of Rs. 1,00,000 on the 21st December 1923 and a further monthly payment of Rs. 750 during the residue of the lease.

On an assessment of this sum of Rs. 1,00,000 for the year 1927-28 as salami or premium assessable under section 12 of the Income-tax Act, the assessee claimed exemption as a capital receipt, casual and non-recurring and further not assessable in the year 1927-28.

Held, that the sum in question was realisation of part of the enhanced value of the assessee's assets consequent on the forfeiture of the lease and hence not assessable.

Case stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal for the opinion of the High Court.

CASE

Under the provisions of section 66 (2) of the Income-tax Act, I have the honour to refer to the Hon'ble High Court certain questions of law arising out of the order of the Assistant Commissioner of Income-tax, Headquarters, on appeal filed by the Gooptu Estates Limited against the assessment made on them by the Income-tax Officer, Companies District, for the year 1927-28.

2. The facts of the case are as follows :—The Gooptu Estates Limited, a Limited Company, have taken lease of certain house properties belonging to Babu Ram Chandra Gooptu deceased, and receive rents from the sub-tenants. The premises at No. 100 Clive Street, are one of these properties. They were leased to the Tata Industrial Bank Limited for fifty years from the 1st August, 1920. It was agreed upon between the Company and the Bank that if the conditions of the lease were breached the lease would at once expire. In the year 1923 the Tata Bank went into voluntary liquidation to effect an amalgamation with the Central Bank of India Limited. This was considered by the company as a breach of the conditions of the lease. Finally they compromised their claim by accepting a lac of rupees, and made over the premises to the Central Bank of India Limited, at an increased rent for the unexpired portion of the lease. This lac of rupees was received on the 21st December 1923, i.e., in the year 1923-24, and was admittedly shown under the head suspense account in the balance sheet for 1923, the accounting year of the Company being the calendar year, but it did not pass through the Profit and Loss Account. The same thing happened in 1924 and 1925 the heading only being changed from "Suspense" to "Lease Account". As the amount was treated as in suspense in the accounts it was not included in the assessment of the Company for any of the years 1924-25, 1925-26 or 1926-27. In the balance sheet of the year ending 31st December 1926 the amount was shown under the "Reserve Account" without, however, passing it through the Profit and Loss Account, as should have been done. In checking the accounts of 1926 this item came to the notice of the Income-tax Officer and the amount was added back to the profits. Thus the amount was for the first time assessed under the head "Other sources" to income-tax and super-tax for the year 1927-28.

3. Against the assessment the Company appealed to the Assistant Commissioner of Income-tax claiming that the said lac of rupees was not income assessable to tax. It was either a casual gain or a capital receipt and so exempt

from tax. Further were it assessable it could not be taxed in 1927-28. The Assistant Commissioner of Income-tax decided that it was *salami* and as such liable to tax in the year 1927-28, for until the amount was shown under the head "Reserve Account" the Income-tax Officer was not in a position to consider whether the amount was assessable or not.

4. Finally the Company have filed a petition under sections 33-66 (2) asking for review of the Assistant Commissioner's order on appeal or for reference to the High Court of the following questions of law:—

- (1) Whether the sum of Rs. 1,00,000, having been received in consideration of the waiver of their rights in connection with a breach by the lessee of a vital condition of the lease, is in the circumstances a casual gain or a non-recurring income within the meaning of section 4, sub-section 3 clause 7, of the Income-tax Act.
- (2) Whether the said sum of Rs. 1,00,000 was a *salami*, and whether even assuming that it was a *salami*, it is an assessable income within the meaning of the Income-tax Act, or is a capital and casual non-recurring receipt as held in the case, *Shiva Frosad Sing v. The Crown* (1).
- (3) Whether the income derived, accrued and received in the year 1923 can in the circumstances, *viz.*, the transfer of the amount from one account to another to suit the convenience of accountancy, be treated as assessable income in the year 1927-28.

I have declined to interfere in review and so refer the case to the Hon'ble High Court. My opinion on the questions is as below:—

Q. 1.—The sum in question is not covered by section 4 (3) (*vii*) of the Act, as it is a receipt arising directly out of the assessee's occupation, which is that of sub-letting leasehold properties. The decision of the Calcutta High Court in the case of *Turner Morrison v. Commissioner of Income-tax* (1) applies.

Q. 2.—The payment was in the nature of a *salami* or premium paid in consideration of the Central Bank being allowed to replace the original lessee, the Tata Bank Limited. Such *salami* or premium is an addition to the Company's profit for the year in question. The ruling quoted by the assessee does not seem to have any bearing on the question.

Q. 3.—It is a question of fact and depends on the circumstances of the case whether the sum in question was assessable in the year 1927-28 or not. Owing to the manner in which it was shown in the accounts the sum was treated as in suspense in the assessments for 1924-25, 1925-26 and 1926-27. When it was for the first time shown in the balance sheet as in reserve in 1926 it was considered to have become part of the Company's profits, and was rightly assessed in the assessment for 1927-28. This hardly involves a question of law.

A. K. Roy, Sukumar Mitter and Susil Sen, for the Assesseees.

Advocate-General and Radha Binode Paul, for the Crown.

JUDGMENT

RANKIN, C. J.:—The assesseees are a limited company (Gooptu Estates Limited) who in 1922 took a lease for fifty years from the representatives of one Ram Chander Gooptu of certain properties which included the premises known as 100 Clive Street, Calcutta. This lease was subject to a building lease previously granted in June 1920, by the executors of the will of the said Ram Chunder Gooptu, where-

by the premises 100 Clive Street were demised for 50 years to the Tata Industrial Bank Limited on a monthly rental of Rs. 5,000. The Tata Industrial Bank Limited had paid a premium or *salami* of 1 lakh of rupees and by the terms of the lease had undertaken to demolish the building then standing on the demised premises and to erect thereon a new office building in accordance with conditions to be approved by the lessors. In August 1923 the Tata Industrial Bank Limited, having expended a large amount of money upon the erection of the new building, went into voluntary liquidation for the purpose of a scheme of amalgamation with the Central Bank Limited. Thereupon the assessee, Gooptu Estates Limited, taking advantage of a forfeiture clause in the lease of 1920 which gave power to the lessors to re-enter if the Tata Industrial Bank Limited should go into liquidation, claimed to determine the lease and demanded immediate possession. The Central Bank of India Limited, faced with this claim, compromised with the assessee who waived the forfeiture and agreed to a transfer of the lease to the Central Bank limited in consideration of a lump sum payment of Rs. 1,00,000 and a further monthly payment of Rs. 750 during the residue of the lease. The sum of 1 lakh was paid by the Central Bank Limited to the assessee on the 21st December 1923. The Income-tax authorities for the year of assessment 1927-1928 have claimed to treat this sum as part of the assessable income of the assessee and the Commissioner of Income-tax, Bengal, has at their request referred to this Court the following questions of law :—

- (1) Whether the sum of Rs. 1,00,000, having been received in consideration of the waiver of their rights in connection with a breach of the lessee of a vital condition of the lease, is in the circumstances a casual gain or a non-recurring income within the meaning of section 4, sub-section 3, clause 7, of the Income-tax Act.
- (2) Whether the said sum of Rs. 1,00,000 was a *salami*, and whether even assuming that it was a *salami*, it is an assessable income within the meaning of the Income-tax Act, or is a capital and casual non-recurring receipt as held in the case, *Raja Shiva Prosad Sing v. The Crown* (1).
- (3) Whether the income derived, accrued and received in the year 1923 can in the circumstances, *viz.*, the transfer of the amount from one account to another to suit the convenience of accountancy, be treated as assessable income in the year 1927-28.

I propose to consider the second question first. The assessment order dated the 30th November, 1927, has been included in the paper book and from this, as well as from the case stated, it appears that the assessment was made under section 12 of the Act under the head "other sources." The assessment order shows that the assessment being under section 12, and not under section 10 under the head "business," the Income-tax authorities have refused to permit the assessee to take credit for any sum on account of depreciation of the buildings. etc., which are part of their capital assets.

In a case of this character much may depend upon the particular head of charge under which the assessee is being brought, and the question before us is not to be decided under section 9, 10 or 11 of the Act. Where the assessee is the owner of property consisting of any buildings or land appurtenant thereto, the statute charges him upon the basis of a notional income the amount of which is computed by finding the *bona fide* annual value and making the deductions therefrom which are allowed by section 9. As the assessee in this case has only a limited interest, namely, the interest of a lessee for fifty years, the Income-tax authorities may well be right in regarding section 9 as inapplicable to the case. Again, if in the view taken by the Commissioner the circumstances are not such that the assessee can be regarded as carrying on a business in house property—a

view which has not been questioned before us and which must clearly be accepted—it is obvious that the assesses cannot be made liable upon principles which are applicable only to persons carrying on business.

If we were dealing with this case under section 10 of the Act, and upon a finding that the letting out of property upon lease for *salami* and for rent, the forfeiting of leases where possible and the exaction of fresh *salami* and increased rent were all acts done in the carrying on or carrying out of a business in house property it might well be correct to hold that the sum now in question was earned as part of the profits of the business, and was assessable accordingly to tax: *Commissioners of Taxes v. Melbourne Trust Limited* (1); *In re Spanish Prospecting Company* (2); *Assets Company Limited v. Forbes* (3). On the other hand on that view the assessee would be entitled to the allowance in respect of depreciation on buildings, machinery, plant or furniture prescribed by clause (vi) of sub-section 2 of section 10.

From this standpoint 'profits' as Lord Moulton observed in *In re Spanish Prospecting Co.* (2), implies a comparison between the state of a business at two specific dates usually separated by an interval of a year, and if the company was to be regarded as dealing in house property by letting it out for premium and rent in the course and for the purposes of its business, the money value of the extent to which at the end of a year it had bettered its position by such means would be assessable as profit. If its position has bettered by other means, from causes not directly connected with the business of the company, the enhanced value though realised is not part of the profits of the business: *Californian Copper Syndicate Ltd. v. Harris* (4); *Tebräu (Johore) Rubber Syndicate Ltd. v. Farmer* (5). Everything depends upon what the business is.

If however the assessee is not carrying on a business the matter must be examined from another angle. The absence of any provision in section 12 of the Act for an allowance of depreciation upon fixed capital is an indication of the difference. It points to the fact that under this head the income can *prima facie* be ascertained without a valuation of all assets at two different dates and by means of a computation of receipts and expenditure into which the rise or fall of capital values does not enter. If the expenditure required to obtain the income from the capital asset is negligible the case is the simple case of a man in receipt of a clear revenue therefrom. If some considerable expenditure is necessary before the annual return can be obtained then the history of the year will be stated in the form of a 'Trading' or 'Revenue' Account or account of the receipts and expenditure during the year. It is essential when accounting on this basis to exclude from either side of the account matters which in substance represent only a rise or fall in the value of the asset from which revenue is derived as distinct from the net revenue itself, or which represent only a change in the form of the investment, whether the change be a change into money or into some other form of property.

Now cases of *salami* or premium upon a lease may present considerable difficulty in maintaining the distinction between capital and revenue accounts. In *Raja Skiva Prosad's case* Dawson Millar, O. J. discussed the question in the case of a holder of an impartible Raj who possessed Zemindari properties. The case before us is the case of a company and apparently of a company which possesses a good many lease-hold properties. But under section 12 of the Act and upon the facts stated in the case I do not see how a different result can be arrived at from that which would have been correct had the lease of 100 Clive Street been the sole capital asset of an individual. Section 12 covers many different types of income but even if it be assumed that such matters would affect the question, the case stated contains no findings as to the character or constitution of the company, the purpose for which

(1) (1914) A.C. 1001.

(3) 3 Tax Cas. 542.

(2) (1911) 1 Ch. 92.

(4) 5 Tax Cas. 159.

(5) 5 Tax Cas. 658.

it was formed, the extent of its operations or the particular character of the transaction by which the representatives of Ram Chandra Gooptu deceased with the assent of the beneficiaries under his will have demised his properties to Gooptu Estates Ltd. We know indeed that the assessee company is not said to be carrying on a business and it may be, for aught we know, that it has been formed merely to provide convenient machinery for management or as a scheme by which the testator's estate can be administered and in the end distributed to the best advantage.

Looking at the assessees therefore simply as owing lease-hold property from which they derive a revenue, we find as regards 100 Clive Street, that they are charged and chargeable under section 12 with the whole of the net rent notwithstanding that it is derived from a wasting asset. They have a lease for fifty years from 1922 and the property is sublet for fifty years from 1921. In 1923 when the Tata Industrial Bank incurred a forfeiture of their lease the assessees instead of being interested merely as reversioners entitled to the rent reserved during the currency of the lease became at one stroke entitled to immediate possession of the property as it then stood. Their investment or capital asset had advanced suddenly in value and they were free to deal with it as they liked, subject only to the covenants in their own lease. Had they sold it no part of the purchase price could have been regarded as revenue. Had they sold a half share in it the same would still hold. What then did they do? By a bargain with the Central Bank they contrived to the extent of a lac of rupees to realise the *enhanced* value at once and the rest of the enhancement in value of their asset they converted into a right to an additional monthly sum of Rs. 750. The finding by the Commissioner is that the lac of rupees was "in the nature of a *salami* or premium" and he adds "paid in consideration of the Central Bank being allowed to replace the original lessee". These last words are not very lucid because the sum was not exacted as a term of mere assent to an assignment but by reason of the claim that the lessee had incurred a forfeiture and in consideration that the forfeiture was waived. The sum in question is certainly to be regarded as a *salami* or premium and that in the ordinary sense. It was demanded and paid in respect of a re-settlement of this property not for a year or even for a few years only but for the remaining 48 years out of the 49 years which exhausted the assessees' leasehold interest. I do not say that *salami* can never be income under Sec. 12 but it would in my opinion be highly unreasonable to treat any part of this *salami* as income. The very logic by which the Act has excluded from the account any allowance for depreciation of this wasting asset excludes this item also. Neither has place in a revenue account, if the account be strictly limited to its immediate purpose.

In my opinion the second question referred to us should be answered in favour of the assessees. In this view the other questions do not arise and need not be discussed.

The assessees must have their costs of the Reference.

GHOSE, J:—I agree.

BUCKLAND, J:—I agree.

(326) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA

*Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose
and Mr. Justice Buckland.*

(12th August, 1929)

Raja Bejoy Singh Dudhuria Assessee.

vs.

The Commissioner of Income-tax, Bengal Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 8, 9, 10 and 12—Assessee paying

maintenance to step-mother—Maintenance charged on entire estate under decree of court—Sums so paid, if deductible.

Where the assessee, a Zemindar governed by the Mitakshara law, on an assessment to income-tax claimed deduction of the amount of maintenance paid to his step-mother under a decree of court charging his entire estate with payment thereof

Held, that treating the maintenance as a charge on each of the heads of the assessee's income assessed under sections 8, 9, 10 and 12 of the Income-tax Act, the claim was not allowable under any of those sections.

Case stated under Sec. 66(2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE

In accordance with the provisions of section 66 (2), I have the honour to refer for the decision of the Hon'ble High Court certain questions of law which arose out of the assessment on Raja Bejoy Singh Dudhuria by the Income-tax Officer, Murshidabad.

The facts of the case are as follows:—The assessee, Raja Bejoy Singh Dudhuria has a step-mother named Srimati Sukan Kumari Bibi. After the death of the assessee's father the step-mother filed a suit in the Calcutta High Court for a declaration that she was entitled to proper maintenance and accommodation for her residence out of the properties in the hands of the assessee, her step-son, and belonging to the estate of her deceased husband. The case was compromised, and under the second term of the Schedule the widow is to receive, and the assessee is to pay, out of the estate a sum of Rs. 1,100 month by month for life for her maintenance. She lives in Bikaner, and the assessee resides in Bengal. The Income-tax Officer, Murshidabad, was assessing the widow through the assessee as her agent. Against the 1924-25 assessment, in which the allowance was classed as salary paid by a private employer and assessed under section 7 (1) of the Income-tax Act, the widow filed an appeal before the Assistant Commissioner, Burdwan Range, claiming that she was not liable to assessment at all. The Assistant Commissioner rejected the appeal. She then filed a review petition before the Commissioner claiming amongst other things that her allowance was not assessable under the head "salary" or under any other head, and that the assessee, her step-son, who paid the allowance, could not be held to be her agent under section 43. On enquiry it was found that the step-son was being assessed as an individual and not as the representative of a Hindu undivided family, and that the allowance paid to his step-mother had been allowed as a deduction in arriving at his assessable income. Not being satisfied with the correctness of these assessments, my predecessor issued a notice on the assessee to the effect that he desired to hear him on the question whether the monthly allowance paid to his step-mother should be allowed as a charge on his estate for the purpose of income-tax assessment. His representative appeared and claimed that the allowance was an annuity, and as such taxable as salary under section 7(1), and that it should be deducted under section 10(2) (iii) read with section 12(2) from the assessable income in the hands of the assessee.

My predecessor disagreeing with this view held that the allowance was not 'Salary', as there was no relation of employer and employed between the assessee and the widow. On the contrary, they are both members of the same Hindu undivided family, of which the former was the Manager, and the latter was entitled to maintenance out of the properties belonging to the joint family. He accordingly cancelled the assessment of the widow under section 33, and under the same section directed that the assessment of the step-son, the assessee in this case, be revised and the deductions hitherto allowed to him in respect of the monthly payments to his

step-mother be included in his total income. I was then asked to myself review under section 33 of the Act this order of my predecessor enhancing the assessee's assessment, or in the alternative to refer the case to the High Court under section 66 (1) to decide whether the order passed by my predecessor was a legal one, and especially whether acting as Commissioner under section 33 of the Act he was entitled to enhance the assessment himself or should have referred it to the Income-tax Officer to do so. I rejected this application as I was not empowered to review my predecessor's order under section 33 and was not prepared to refer any alleged question of law to the High Court under section 66 (1).

The assessment on the assessee in the present case, Raja Bejoy Singh Dudhuria was then made in accordance with the order under section 33. Dissatisfied with this revised assessment the assessee again appealed to the Assistant Commissioner, Burdwan Range, under section 30. The Assistant Commissioner rejected this petition of appeal, as he considered the revised assessment by the Income-tax Officer to be quite legal.

The assessee has now asked for a reference to the Honourable High Court under section 66 (2) of the Income-tax Act on nine questions of law quoted below:—

- (1) Whether the Commissioner has any jurisdiction to himself make an assessment on your petitioner under section 33?
- (2) Whether the learned Commissioner was wrong or not in enhancing the assessment under section 33 without hearing your petitioner on the specific subject of enhancement?
- (3) Whether the Commissioner acted with material irregularity or not in straying beyond the point for settlement as indicated in his letter No. 5980 C. T., dated 5th January 1926, and deciding upon altogether different point which does not arise in a case like this?
- (4) Whether the Commissioner acted legally in ignoring the documentary evidence which would show that your petitioner is the sole heir to the estate of his deceased father, and the said Srimati Sukan Kumari not being a member of your petitioner's joint family, was entitled only to what has been awarded to her by the decree of the High Court, dated 23rd May 1922?
- (5) Whether it should have been held that your petitioner is entitled to the exemption as claimed by him?
- (6) Whether having regard to all the facts and circumstances your petitioner and Srimati Sukan Kumari Bibi can be treated as members of a Hindu undivided family?
- (7) Whether reassessment under the circumstances of the case can be made without following the provisions of section 34 of the Act read with sections 23 and 22 of the Act?
- (8) Whether any demand under section 29 can lawfully be made in these circumstances, and what is the scope of section 29 of the Act?
- (9) Whether in assessing the annual value of your petitioner's property the sum of Rs. 9,900 payable by your petitioner to Srimati Sukan Kumari Bibi has to be deducted or not?

The first of these questions, viz. "Whether the Commissioner has any jurisdiction to himself make an assessment on your petitioner under section 33" is based on a misapprehension or mistake of fact. The Commissioner is not an assessing

authority under the Act, and the assessment in this case was made not by the Commissioner but by the proper assessing authority, the Income-tax Officer, in accordance with the Commissioner's order passed under section 33.

Questions 2, 3, 4, 5, 6 and 9 do not arise out of the Assistant Commissioner's order under section 31 passed on 13th May 1926, as the Assistant Commissioner did not discuss these points in his order. Presumably he considered that as these points had been decided by the Commissioner himself in a review case, in which the present assessee was the petitioner, it was not within his province to discuss them, though the same or similar points were raised in the appeal petition. It seems that he was right as it can hardly have been the intention of the framers of the Act that an appeal should lie to the Assistant Commissioner on questions already decided by the Commissioner himself. If, as I hold to be the case, revised assessments made in accordance with orders passed under sections 31, 32, 33 and 66 (5) are actually made under section 23 read with one of these sections, then an appeal will lie to the Assistant Commissioner if the revised assessment is made under a subsection of section 23 which ordinarily admits of an appeal. But such an appeal can surely only lie to the Assistant Commissioner on fresh points arising out of the assessment, and not on any point already disposed of by the Assistant Commissioner, the Commissioner, or the High Court, as the case may be.

In regard to question (2) it may be added that it involves a misstatement of fact as in the Commissioner's order of 24th March 1926, to which reference is made, I find the following sentence "in accordance with the proviso to section 33 the assessee was heard on 26th January 1926 before this order prejudicial to him was passed." This is corroborated by paragraphs 5 and 6 of the present petition.

Questions 7 and 8 run as follows :—7. Whether reassessment under the circumstances of the case can be made without following the provisions of section 34 of the Act read with section 23 and section 22 of the Act? 8. Whether any demand under section 29 can lawfully be made in these circumstances, and what is the scope of section 29 of the Act? These questions may be said to arise out of the Assistant Commissioner's order of 13th May 1926, and I accordingly refer them for the decision of the Hon'ble High Court and give my opinion in regard to them, as I am required to do.

Question 7. The objection seems to have its origin in the circumstance that the Income-tax Officer, at the head of the assessment form, of which the demand notice subsequently issued was a copy, described the assessment as a revised assessment under section 33 of Act XI of 1922 instead of as a revised assessment under section 33 read with section 23 (3) of the Act. It is quite true that section 33 is a reviewing and not an assessing section, but its wording clearly gives the Commissioner power to direct the revision of an assessment, and in the absence of any definite instructions in the section itself as to how such revision is to be carried out, we must presume that the Commissioner's orders will be put into effect by the Income-tax Officer with the help of the ordinary assessing procedure, *viz.*, that prescribed in section 23. Similarly when an assessment is revised in accordance with orders passed under sections 31, 32 or 66 (5) the Income-tax Officer, as the assessing authority, makes the revised assessment under one of these sections read with one of the subsections of section 23. In such cases there is no question of calling for a return under section 22(2) unless the superior authority directs the Income-tax Officer to do so or directs him to take action under section 34.

I do not consider that the omission to add section 23 (3) in the heading of the assessment form in this case in any way invalidates the revised assessment made by the Income-tax Officer.

Section 34 is not the appropriate section for the Income-tax Officer to use when making a revised assessment in accordance with the Commissioner's order

under section 33. The wording of the section makes it sufficiently plain that it is primarily intended to enable the Income-tax Officer to himself take action to assess or reassess any income, profits or gains, which may have escaped assessment in any year or have been assessed in that year at too low a rate, without taking the sanction of any higher authority to do so.

From paragraph 7, sub-paragraphs (a) and (b) of this petition it is evident that the petitioner means that when an assessment is ordered to be revised by the Commissioner under section 33 his orders can only be put into effect by the Income-tax Officers taking action under section 34. But, when as not infrequently happens, the revision by Commissioner has the effect of reducing an assessment, section 34 is obviously inapplicable. What then should be the procedure in such cases?

In the particular case with which we are concerned the Commissioner disallowed an expense which had been allowed by the Income-tax Officer, and in the revised assessment this expense was added back by the Income-tax Officer. Such a transaction can hardly be described as the assessment of income, profits, or gains which had escaped assessment within the meaning of section 34 and, to my mind, that section is not applicable to the case.

Question 8. If, as explained above, an order of the Commissioner under section 33 of the Act directing the revision of an assessment is subsequently put into effect by the Income-tax Officer under section 33 read with one of the sub-sections of section 23, then the issue of a demand notice under section 29 of the Act naturally follows, and no question of irregularity arises. It is true that there is no mention of section 33 in section 29, but neither is there any mention of sections 31, 32 or 66 (5). Yet when the orders passed under those sections have the effect of revising an assessment a fresh demand notice must be issued on the assessee.

JUDGMENT

RANKIN, C. J.:—The question in this case arises out of the assessment to income-tax made upon Raja Bejoy Singh Dudhuria of Azingunj in the year 1924-25 and the year of account is 1923-24.

The assessee submitted a return of his income in the ordinary way as an individual and the Income-tax Officer on the 16th of March 1925 assessed him at a figure of Rs. 1,12,005 after allowing him a deduction of Rs. 9,900 in respect of the fact that he had paid a sum of Rs. 1,100 per month to Sreemutty Sukan Kumari Bibi, his step-mother. This sum of Rs. 9,900 represented the proportion of the amount so paid by the Raja attributable to his assessable income as distinct from his agricultural income which is not liable to income-tax. The deduction was attributable to several heads of assessable income as follows:—

	Total income.	Deductions.	Net income.
Interest on securities	8,040	633	7,407
Property	36,110	2,970	33,140
Dividends	9,317	728	8,589
Business	66,611	5,420	61,191
Other sources	1,827	149	1,678
	<u>1,21,905</u>	<u>9,900</u>	<u>1,12,005</u>

The Raja made no objection to this assessment but in January 1926 the Commissioner of Income-tax, Bengal, reviewed the assessment under section 33 of the Income-tax Act, and, after notice to the Raja, and after hearing him came to the

conclusion that the deduction of Rs. 9,900 which had been allowed should be disallowed; and directed that he be assessed on a total income of Rs. 1,21,905. The occasion for this review of the original assessment was an objection by Sreemutty Sukan Kumari Bibi to an assessment made upon her in respect of the maintenance allowance of Rs. 1,100 per month before mentioned. It would appear that the lady lives at Bikaner but that the Income-tax Officer at Murshidabad purported to assess her through the Raja as her agent and had made an assessment upon the monthly sum of Rs. 1,100 on the footing that it was an annuity taxable as salary under the first sub-section of section 7 of the Act. The lady very naturally objected that the Raja was not her employer and the Commissioner very properly accepted this contention. Apart from this, however, the lady maintained that she was not liable to be assessed at all and the Commissioner of Income-tax, in accordance with a contention pressed upon him on behalf of the lady, held that the Raja and she were both members of an undivided Hindu family of which the Raja was the manager. Accordingly he cancelled the assessment on the lady and added to the Raja's assessment the sum of Rs. 9,900.

The Raja took diverse exceptions to the Commissioner's order. Some of these exceptions had reference to questions of procedure; others were on the merits. The Raja contended that he was liable to be assessed as an individual and that he and the lady were not members of an undivided Hindu family. He maintained that the deduction originally made by the Income-tax Officer was a deduction to which he was entitled.

In February 1927 the Commissioner of Income-tax made a reference to this Court upon two questions of procedure and gave reasons why the other questions which he had been asked by the Raja to refer were not, in his opinion, proper to be referred by him. Upon this reference coming before the Court, the Court exercised its power under clause 4 of section 66 of the Act and, by consent of Counsel on behalf of the assessee and on behalf of the Crown, sent the case back to the Commissioner directing him to find the necessary facts to enable the Court to decide "whether it should have been held that the Raja was entitled to the exemption claimed by him"—in other words to decide the merits of the matter. Accordingly the Commissioner in November 1928 has stated the facts and given his opinion upon this question.

According to the case stated, the Raja is by caste a Jain and is governed by the Mitakshara school of Hindu law. His father, Rai Bishen Singh Dudhuria Bahadur died in 1894 leaving him surviving his only son (the Raja) and a widow, Sreemutty Sukan Kumari Bibi who is step-mother of the Raja. At the time with which we are concerned the Raja had no son though a son has since been born to him. Rai Bishen Singh Bahadur appears to have died intestate. He left considerable properties, and some time after his death the widow brought a suit in this Court against the Raja claiming maintenance and suitable accommodation for her residence out of the properties which had belonged to her deceased husband. This suit was compromised and by the consent decree the Raja was directed to make over to her a certain house for her residence and to pay out of the estate the sum of Rs. 1,100 per month for maintenance together with certain arrears of maintenance. The Raja has been regularly paying the monthly allowance as decreed and in the year of account with which we are concerned, he paid in all for this purpose Rs. 13,200. It is agreed that Rs. 9,900 represents the same proportion of Rs. 13,200 as the assessed income of the Raja bears to his total income including agricultural income. In these circumstances the Commissioner is of opinion that the Raja and the lady are members of an undivided Hindu family and that the total income of the family is assessable in the hands of the Raja as manager thereof, no deduction being permissible in respect of the maintenance paid to one of the members. Further, and in the alternative, he is of opinion

that the maintenance paid to the widow is on the same footing as the maintenance provided by the assessee for his wives and daughters and is a personal expense of the assessee and cannot be held to be a charge upon his estate for the purposes of assessment to income-tax.

At the hearing before us the learned Advocate-General abandoned the contention, which found favour with the two Commissioners of Income-tax who have dealt with the case, that the Raja and the widow were members of an undivided Hindu family. He accepted the position that the Raja was liable to be assessed as an individual and in no other manner. He contended, however, that on this footing there is no provision in the Act by which he can claim to deduct a sum of Rs. 9,900 on the ground that it had been paid by him to his step-mother for her maintenance.

The decree of the High Court in the suit by the widow against the Raja has not been included in, or made part of, the case stated by the Commissioner or of the additional statement of facts made by him. In the Raja's petition to the Commissioner of Income-tax it is stated that "by the said decree the payment of the said sum was made a charge on your 'petitioner's estate'", but this very important fact has been omitted from the case stated. Before us, however, it was not disputed that the lady's maintenance was a legal liability of the Raja arising by reason of the fact that the Raja is in possession of his ancestral estate, that it is payable out of such estate and that this Court had declared that the maintenance was a charge thereon in the hands of the Raja. The general Hindu law upon this subject has been laid down in the case of *Baidya v. Nutha Govindlal* (1). The position therefore is, and the case must in my judgment be dealt with on the footing, that the lady has a charge which extends not only to the zemindari property of the Raja but covers each of the five heads of property between which it was allocated in the original order of assessment dated the 16th March, 1925.

In these circumstances I am not of opinion that anything turns upon the fact that the person entitled to the benefit of the charge is the Raja's step-mother. It has been suggested in argument, and the suggestion finds place in the Commissioner's observations in the case stated, that substantially speaking, and upon the question of merits, the Raja's liability to provide maintenance for his step-mother is of the same kind as his liability to provide for his wives and daughters. This contention is I think unsound. We are proceeding on the footing that the Raja is to be assessed as an individual. Whether this be right or wrong, it is the common case of the parties before us, and on that footing the Raja's position is, I think the same as if he had received his various properties, securities and businesses under a bequest from his father upon the terms that those assets were charged with an annuity for the maintenance of the widow. We are not dealing here with a charge created by the Raja for the payment of debts which he has voluntarily incurred. The Raja is by virtue of an exceptional and peculiarly extensive charge an owner of incumbered property and the question before us requires us to ascertain the law applicable to a case where the income from property, securities, business, etc. is subject to a charge for an annual sum. In the present case it would doubtless have been open to the Court, had circumstances required it, to raise and set apart out of the estate a capital sum to answer the right of the widow to her annual maintenance (See *Hemanginee Dasse v. Kumode Ch. Das* (2), and in any case, should default be made in paying the annual sum, it would be open to the Court, in a suit to enforce the charge to appoint a receiver of the properties and give him directions, if necessary, for sale of a sufficient portion thereof. I do not think, however, that the present question is complicated by the fact that the lady's charge is not confined to the income of the estate but extends to the corpus. Where the income is

(1) I. L. R. 9 Bom. 279.

(2) I. L. R. 26 Cal. 441.

sufficient, it is clearly the usual business course to meet this claim out of the income. A similar question was raised and dealt with by Lord Macnaghten in his speech in the House of Lords in *Attorney-General v. London County Council* (1). The cases are not absolutely on all fours, but in this case it seems to me that it would be paradoxical merely because the lady can, in case of default, resort to the corpus of the property, to say that it is right and proper, before default and merely for the purpose of computing income-tax, to treat her annuity as payable rateably out of the capital and the different branches of the income.

What then is the provision made by the Indian Income-tax Act, (XI of 1922) as regards the liability to tax of a person whose income is incumbered in this way with the payment of an annuity? The fourth clause of sub-section (1) of section 9 deals with a similar matter, but the scheme of the Act, with reference to cases of this type, is by no means easy to discover. In the speech of Lord Macnaghten in the case to which I have already referred, there is a short account of the manner in which this question has been treated by the English Income-tax Acts. From this it would appear that the English Acts have always dealt with this question in express terms. Before 1803 there was a provision for deduction of such payments. After 1803 such deductions were prohibited and the tax-payer liable to an annual payment was authorised to deduct and retain the tax upon the payment which he was bound to make. It seems to be clear that in England the principle of taxation at the source would be employed. In a case like this, the tax-payer liable to pay the annuity would pay upon the whole of his income without deduction therefor but would be entitled to pass on the incidence of the tax by deducting the amount thereof when he made payment to the annuitant. Under the Indian Act taxation at the source is not unknown. Firms are taxed and the partner is not charged again upon his share of income; companies are taxed and the shareholder is not charged again upon his dividend; Hindu undivided families are taxed and the individual member is not charged again upon his share. Again deduction of tax at the source is provided for by section 18 in the case of salaries and interest on securities, the payer being authorised and required to deduct the tax and himself to make payment to Government of what he has deducted. The present case is wholly untouched by any of these provisions. Accordingly a good many considerations have to be weighed before it can be decided whether the owner of property or business or securities subject to a charge for annuity can get any allowance in respect of his liability. Assuming for the present purpose, and contrary to the contention of Sreemuthy Sugan Kumari Bibi, that we are not here dealing with the case of an undivided Hindu family, and assuming further, without deciding, that the lady, although a resident of Bikaner, is chargeable under the Act, her case would seem to come within the provisions of section 19 and tax on her income to be payable by herself direct. No doubt machinery is provided by sections 40 to 43 whereby the assessment might be made upon a trustee in British India; but even if the Raja can be deemed her agent or trustee, the basis of any such assessment would be that the lady's income was being assessed in effect upon herself. We are solely concerned with the Raja's own liability to be assessed upon the sum in question as part of his own income. "If the Crown, seeking to recover tax, cannot bring the subject within the letter of the law, the subject is free"—Per Lord Cairns in *Partington v. Attorney-General* (2). But the Court cannot undertake out of its own notions of what is fair, to adapt or rearrange the machinery of the Act upon a matter of this character and importance.

If each head of income in this case be taken separately and the annuity regarded as a charge upon each, the case would stand as follows: As to interest on securities under section 8, the question is whether the whole amount brought to charge is "interest receivable by him." I cannot

(1) 5 Tax Cas. 292.

(2) (1869) L. R. 4 E & I. App. H L 100 at page 122.

see that there is any provision which would enable the assessee to make a deduction in respect of this annuity. As to dividends the charge falls upon "any sum which he receives by way of dividend" [sec. 14 (2)]. The same reasoning applies to this. As income-tax is deducted at the source or taxed at the source in these cases the assessee if he established a right to treat any part of the income as belonging to the lady and not received or receivable by himself would gain no advantage except for super-tax purposes or unless it made a difference to the rate of charge.

As regards property, under section 9, the first question is whether the Raja is the owner of the property. If he be the owner, as he certainly is, then the charge is to be upon him on the basis of the *bona fide* annual value less certain deduction specially provided for. Clause 4 says "where the property is subject to a mortgage or charge or to a ground rent, the amount of any interest on such mortgage or charge or of any such ground rent" may be deducted. These words cannot in my opinion be stretched to include the present case. The departure from the language of the English Acts is very noticeable here. The object of the legislature in making this provision may have been any one of many different things. It may, for example, be a recognition of the fact that it is common to buy property with borrowed money raised on security of the property so bought.

Under section 10, the first question is whether the Raja is a person who carries on a business. If so, he is liable according to the section and in my opinion it is clearly impossible to make room for a deduction on the ground that he has to pay this annuity out of the profits. *Prima facie* the destination of profits is irrelevant.

Under section 12, as regards "Other sources" the language employed by the legislature is less precise. The provision for deduction gives a right to the assessee to "an allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee." This annuity cannot in my opinion be regarded as a personal expenditure of the assessee treating him as an individual whose property is subject to a charge for this annuity. But the payment does not otherwise come within the exception. It may be said that the income, profits and gains mentioned in sub-section (1) means, when read with section 3 of the Act "income, profits and gains of the individual" namely of the assessee and that under this section a deduction might be made upon the general principle that money payable to the lady is not income of the Raja. It happens that the total income of the Raja under this head is small, namely Rs. 1,678. I do not think, however, that on this ground the deduction can be allowed either under section 12 or under any other section. In *Attorney-General v. London County Council* (1), Lord Davey, with reference to sections 60 and 102 of the Income-tax Act of 1842, said "It is not open to doubt, and was not disputed, that sections 60 and 102 alike mean that the person paying a yearly interest may deduct and retain the amount of the tax for his own benefit, and the scheme of the Act is so far clear, and is in favour of the tax-payer. It was no doubt considered that the real income of an owner of encumbered property, or a property charged (say) with an annuity under a will, is the annual income of the property less the interest on the incumbrance or the annuity; and the mortgagee or annuitant and the owner of the property are, in a sense, entitled between them to the income".

Lord Davey in this passage is giving expression to a principle which he finds applied in the sections which he is construing. He is not saying that this is a principle to which Income-tax Acts are to be made to bend or even a presumption

that is to be imported into them where this is not impossible. In the case stated there is no information as to the nature of the "other source" the income of which is assessed at Rs. 1,678. The assessee has made no specific case upon this head and it would, I think, be wrong to apply Lord Davey's language blindly or in the dark to this head of income. Cases under this head may be of almost any kind. Suppose for example the income in question comes from the letting out of lease-hold property upon agreements made with the assessee for a monthly rent to be paid to him by the sub-tenants; could it be said of the net rents so produced that in part or in whole they are not "income, profits or gains" to him because his father's widow has a charge for her annuity upon all the assessee's property? I think not. It may in a sense be true that income is not "real income" unless the individual in question is able to control it for his own purposes or to absorb for himself the whole of the benefit thereof. But I do not see that the Court can in interpreting this Act engage to give it the result required by this line of argument. Nor that the annuitant in a case like this case be regarded as joint owner of the income in a legal sense consistently with the machinery and purposes of the Act.

Into the questions which might arise if an attempt were made by the Income-tax authorities to recover tax a second time from the lady, we are not required to enter. As this decision is being given upon a footing to which the parties before us have agreed but from which as I understand the lady dissents, it is inadvisable upon this aspect of the matter to say anything here.

In my opinion the question whether it should have been held that the assessee was entitled to the exemption claimed by him should be answered in the negative, but having regard to the position taken at different times by the Income-tax authorities I am of opinion that the assessee is entitled to the costs of this case stated.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(327) IN THE HIGH COURT OF JUDICATURE AT RANGOON

*Before Sir Benjamin Heald, Kt., Offg. Chief Justice,
Mr. Justice P. N. Chari and Mr. Justice Ormiston*

(12th August, 1929)

C. T. V. S. Chettyar Firm *Assessees.*

vs.

The Commissioner of Income-tax, Burma *Referring Officer.*

Indian Income-tax Act (XI of 1922) Secs. 13, 33 and 66(2)—Money lending business—Estimate computed on total capital, and not on actual interest receipts—Assessment for subsequent year on actual receipts—Double assessment—Review by Commissioner during reference application.

The assessee a firm carrying on money lending business, were assessed for the years 1925—25, and 1925—1926 under Sec. 13, proviso of the Income-tax Act on an estimate income reasonably expected to be earned by their total capital less deduction for borrowed capital and expenses, and not according to the income shown in their account books. On an assessment for 1926—27 based on actual interest receipts in

in the account books the assessee contended that the assessed sum included interest assessed in previous years as having accrued in those years and not assessable again. The contention was overruled on the ground that the previous years' assessments having been made on a method of averages, there could be no double assessment. On a reference to the High Court,

Held, that where the computation of income had been made in a particular year under Sec. 13, proviso the assessee was entitled to show that income included in the assessment for a subsequent year was included in that computation and that this question was one of fact to be determined on the evidence in the particular case.

Case [Civil Reference No. 9 of 1929] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma for the opinion of the High Court.

CASE

In accordance with the order dated the 25th March 1929 of the High Court of Judicature at Rangoon in Civil Miscellaneous Application No. 129 of 1928,* the

* Judgment of HEALD and OTTER, JJ. :—

HEALD, J.:—Applicants who are the C. T. V. S. Chettyar Firm were assessed for income-tax on an estimated income of Rs. 10,030 for the year 1924-25. For the year 1926-27 they submitted a return showing a loss of over Rs. 45,000. They said that the actual income from their business for the two years 1924-25 and 1925-26 was Rs. 10,250 and that in view of the fact that for those two years they had paid on an estimated income of Rs. 56,138 they had already paid on an excess of more than Rs. 45,000 over their actual income. They produced certain accounts and a statement which showed their actual income for 1925-26 as Rs. 1,795 and another statement which showed their loss as Rs. 3,877-10-0. The Income-tax Officer rejected these statements on the doubtful ground that although an assessee can file a revised return he cannot file revised statements. On an examination of the accounts for the year 1925-26 the Income-tax Officer found that appellant's income for that year was Rs. 36,654. That assessment was based on a calculation of interest which had actually accrued due during that year in the case of transactions with other Chettyars and interest which had been actually received in that year in the case of transactions with customers other than Chettyars. Applicants objected that part of the sums which on that method of calculation represented the actual interest received from non-Chettyar customers during the year 1925-26 had already been assessed to income-tax in that year and in the previous year, because in those years the amount entered on account of interest from non-Chettyar creditors was based on an estimate and not on actuals and that estimate included interest earned, but not yet received in the year of assessment. The Income-tax Officer rejected this contention and assessed applicants on Rs. 36,654 for 1926-27.

Applicants appealed to the Assistant Commissioner of Income-tax who said that it was obvious that so much of the interest receipts from non-Chettyars as accrued in the previous years must have been taxed already in those years and that to include those receipts in the present assessment would be tantamount to double taxation. He accordingly returned the proceedings to the Income-tax Officer for enquiry and report as to the amount of interest from non-Chettyars which accrued in the previous years and which was included in the assessment for 1926-27. The Income-tax Officer reported that the amount of interest from non-Chettyars which accrued in the previous year and was actually received in 1925-26 was Rs. 34,876 but the Assistant Commissioner said that on further consideration he found that the estimates made for the two years 1924-25 and 1925-26 were not

following case is stated for the decision of the High Court under the provisions of section 66 (3) of the Indian Income-tax Act.

2. The relevant facts of the case are as follows :—

The applicant-firm carries on a money lending business at Ma-ubin. For the assessment for 1924-25, the firm submitted a return and produced certain account books (a Journal and two Ledgers). The account books were examined by the Department and from the data available therein the income for the previous year (the

strictly assessments on what is known as the "accrued" basis but mere assessments on the best data available and that therefore there was no conclusive proof that the sum of Rs. 34,876 had been included in the assessment for the previous years. He accordingly dismissed the appeal. Applicants then applied to the Commissioner of Income-tax to state the case and refer it to this Court under the provisions of section 66 (2) Income-tax Act. The Commissioner refused to state and refer the case and at the same time he passed an order dealing in review with the Assistant Commissioner's orders. Applicants now ask us for an order under section 66 (3) of the Act requiring the Commissioner to state and refer the case to this Court. The only question which is at present before us is whether a question of law arises out of the Assistant Commissioner's order.

It seems to me clear that a question of law does arise, that question being whether in a case where an assessment has been made not on actual receipts but on estimated receipts during the previous two years, and the basis of assessment for the third year is changed to a basis on actual receipts, the assessee is entitled to show that the actuals which are taken as the basis of the assessment for the third year that is, in the present case the year 1926-27, include sums which were included in the estimates for the earlier year or years, on which income-tax was paid for those years. It seems clear that if the income-tax has in an earlier year already been paid on amounts actually received in a later year, income-tax cannot be charged on those receipts in the later year, and it does not seem to me to matter whether the Income-tax authorities choose to call the assessment for the year or years in which the tax was actually paid on those amounts an assessment on the "accrued basis," or an estimate on the best data available. In either case, the basis of the assessment is admittedly an estimate and the question of law seems to me to be whether or not the assessee is entitled to show that receipts for the later year have in fact been included in the estimate or estimates for the earlier year or years. I would therefore require the Commissioner to state and refer the case under the provisions of section 66 (3), Income-tax Act. The cost of the present application should abide the orders of this Court on the reference.

OTTER, J.:—This is an application under section 66 (3) Income-tax Act, 1922, asking this Court to require the Commissioner to state a case upon a question of law for reference to this Court. The short history of the matter is that on 29th January, 1927, by an order of the Income-tax Officer, Maubin, the applicant-firm was assessed to income-tax for the year 1926-27 on the sum of Rs. 36,654 in respect of income for that year. The assessment for that year was made so far as non-Chettyar customers were concerned upon the basis of cash receipts from them during that year. The figure arrived at by the Income-tax Officer for such receipts was Rs. 79,716. It was objected by the applicants that included in that sum was an amount of about Rs. 39,000 which had already been assessed to income-tax in the two preceding years. In these years, viz. 1924-25 and 1925-26, the assessment was said to have been made on what is known as the "accrued basis". For the year 1926-27 the basis of calculation was altered and as I have said, the applicant-firm was assessed for the non-Chettyar receipts upon a cash basis. Upon an appeal to the Assistant Commissioner the latter

Tamil year Ruthirothkari—13th April 1923 to 12th April 1924) was estimated at Rs. 19,030 and the applicant-firm was taxed on this sum. The method of computation (followed also in computing the income for 1925-26) will be explained later. For the assessment for the following year, 1925-26, the applicant-firm submitted a return showing a loss of Rs. 21,380. In response to a notice under section 23 (2), the managing partner of the firm produced three books of account (a Day Book and two Ledgers) for the year Rakthakshi—13th April 1924 to 12th April 1925, the Tamil accounting year for the 1925-26 assessment. These account books were not accepted by the Income-tax Officer who, acting under the proviso to section 13 of the Act, computed the income on the basis described below. The total capital, including shop capital, surplus capital and borrowed capital, employed by the applicant-firm in the business was determined.

by an "interim order dated 23rd March 1927 returned the proceedings to the Income-tax Officer for enquiry and report as to the amount of interest from non-Chettyars which accrued in previous years and which had been included in the sum of Rs. 79,716" and adjourned the appeal. The Income-tax Officer reported the correct figure to be Rs. 34,876 on 27th April, 1917; the Assistant Commissioner passed final orders dismissing the appeal. In the course of that order he stated that he found that the accountant's description of the previous assessments on "accrued basis" was not strictly correct. It should be stated that it is said that an assessment on "accrued basis" means an assessment upon amounts due but not necessarily paid during the period in question. The Assistant Commissioner went on to say that after a return by the applicants had been filed (for the year 1924-25) the firm's books were called for and after extracting certain figures from the books certain calculations were made according to the system then in vogue, it was reported that the assessable income was Rs. 19,630. This figure was accepted by the Income-tax Officer and assessment was made accordingly. According to the Assistant Commissioner this method was in reality an estimate on the best data available. For the following year according to him, after the return had been filed by the applicant-firm certain figures were again extracted from the account books, and after making certain calculations according to the same system as in the previous year, the accountant reported the assessable income as Rs. 37,188 and assessment was made accordingly on this figure. Here also, according to the Assistant Commissioner "it was an estimate on the best available data". This Officer went on to say that "it could not rightly be called the accrued basis. It follows therefore that there is no conclusive proof that the amount of Rs. 34,876 had been taxed in the previous year". He, therefore, was unable to exclude this amount from the assessment for 1926-27.

On 26th May, 1927, the applicant's firm applied under section 66 (2) of the Act to the Commissioner of Income-tax praying that certain questions of law arising out of the appellate order of the Assistant Commissioner should be referred to this Court. On 19th August and 16th September, 1927 respectively, notices were issued by the Commissioner of Income-tax, to the assessee under section 83, Income-tax Act, calling upon them (apparently) to make any representation they wished to make in respect of a proposed revision of their assessment. On 5th March 1928, the Commissioner modified the orders of the Assistant Commissioner, dated 23rd March, 1927 and 27th April, 1927 by passing an order rejecting the appeal of the assessee dated 26th February, 1927 on the ground "that the assessments for the previous years having been computed on a method of averages, the sum in question viz. Rs. 39,000 . . . has not been subject to double assessment." In other words he held that as the method adopted was not "accrued basis" but a basis he called a "method of averages", as a matter of fact the Rs. 39,000 was not and could not have been doubly assessed. He seems also to have thought that the Assistant Commissioner would be bound by his conclusion contained in the adjournment order of 23rd March, 1927 and he therefore "modified" this order and that of 27th April, 1927. On 7th March, 1928

An average rate of interest on this capital was assumed, the assumed rate being a net figure which provided for bad debts etc. From the estimated interest on this capital the interest on borrowed capital *plus* other expenses (either actual or estimated, according to the evidence available) was deducted and the net amount was taken as the assessable income. This method of estimating income is described in the proceedings as "the accrued basis method" but it should be noted that it is a method of estimating income and not a method of computing income from accounts kept on an approved system. On this method the income of the applicant-firm for the assessment for 1925-26 was estimated to be Rs. 37,188 and tax was recovered on this sum.

For the assessment for the following year, 1926-27, which is the assessment in dispute, the applicant-firm filed a return with an explanatory statement declaring a loss of Rs. 45,888. An amended statement was filed later declaring a profit of Rs. 1,795 and later still a further amended statement was filed declaring a loss of Rs. 3,887.

the Commissioner of Income-tax passed orders upon the application preferred by the applicant-firm on 26th May, 1927 and said that none of the questions he was asked to refer could be said to arise and refused to state a case for this Court.

I observe that the applicant-firm had objected to the revision proceedings initiated by the Commissioner but these objections were overruled in the order which is not before the Court. The Commissioner deals with these objections at length. He also says (as I understand at the end of para 6 of his order) that as the figures for 1924-25 and 1925-26 were taken from assessee's books which were kept on a cash basis (and not on accrued basis) no double taxation took place. Later he makes a statement that I cannot follow *viz.*, "as regards the first objection, I do not think that it can be contended seriously that the question whether or not the assessment in the previous years was made on accrued basis is a question of fact". He may not have meant to say this, but if of course this is a question of law it should be stated for this Court.

It seems to me, however, that the matter should be put differently *viz.*, as a matter of law, can not the assessee be allowed to show not necessarily that his assessment was made on one basis or another, but that in fact from figures he has been doubly assessed. In other words, is the applicant not to be allowed to show (if he can) that the total of the estimated income of the firm for 1924-25 and 1925-26 *plus* the actual income for 1926-27 in fact exceeded the total actual income for those 3 years. The Commissioner then deals with the objection that revision proceedings cannot be opened by the Commissioner in a case where an application is pending under section 66 (2) of the Act. He decides that such an application is no bar to proceedings under section 33. But surely this is a question of law. He can only pass orders subject to the provisions of the Act (sub-section 2) and it might be argued that when the Act provides a remedy for an assessee, action should not be taken by the Commissioner until it is decided whether such remedy is available or not. It is true that the proviso to sub-section (2) of section 66 may provide an answer. But it might also be argued that action by a Commissioner under section 33 which cannot (apparently) be called in question by this Court might shut out an assessee from his remedy under section 66 (2).

I think, therefore, that the Commissioner must state a case for our decision upon the following questions of law: (1) Is the applicant-firm entitled to show that the income upon which he was assessed for the 3 years in question exceeded the income actually received in those 3 years? (2) Can the Commissioner during the pendency of an application under section 66 sub-sections 2 and 3, Income-tax Act, take up under section 33 of the Act proceedings which are the subject of the said application?

The accounting year for the 1926-27 assessment was the Tamil year Krodhana beginning on the 13th April 1925 and ending on the 12th April 1926. The period covered portions of two agencies, the old agency (beginning in 1923-24 and terminating on 6th June 1926) and the new agency (beginning on 8th November 1925). The following books were produced:—*Old Agency*:—Two Journals from 16th April 1925. One Chettyars' and two Customers' Ledgers. *New Agency*:—One Journal from 8th November 1925. One Chettyars' and two Customers' Ledgers. The computation of the income for this assessment was made from the books produced and according to the method of accounting followed by the applicant firm. This method is commonly known as the "combined" basis, i. e., partly "cash" and partly "mercantile" or "accrued". On this method all transactions with non-Chettyars, that is, the vast majority of the persons to whom loans are made, are recorded on the "cash" basis, while transactions with members of the Chettyar community consisting mainly of borrowings to supplement the capital of the business are recorded on the "mercantile" or "accrued" system, that is, interest payable on borrowings is debited to the account at stated intervals whether it is actually paid out or not and similarly credit is taken for monies receivable whether they are received or not.

The taxable income determined for the year on this basis was Rs. 34,654 and tax on this amount was recovered.

3. The applicant-firm then appealed to the Assistant Commissioner against this assessment, the ground of appeal relevant to this reference being that in assessing it on the new basis for the year 1926-27, the Income-tax Officer included interest receipts from non-Chettyars amounting to Rs. 39,000 which had accrued in previous years and which, according to the applicant-firm's contentions, had been included in the assessable income of those years. The Assistant Commissioner in an interim order admitted this contention and sent the case to the Income-tax Officer to report what part of the sum of Rs. 79,716 shown as receipts in the accounting year Krodhana and included in the assessment for 1926-27 represented interest which accrued in the previous accounting years. The Income-tax Officer reported this sum to be Rs. 34,876. The Assistant Commissioner, however, on further consideration found that he was not right in assuming that the previous assessments were made on what is described in the proceedings as the "accrued" basis and that in point of fact the assessments for the previous years were not based on the accounts of the applicant-firm. He accordingly rejected the applicant-firm's claim that there had been double taxation in respect of the disputed sum of Rs. 39,000.

4. The applicant-firm thereupon made an application under section 66 (2) asking the Commissioner to refer to the High Court eleven questions purporting to be questions of law arising out of the Assistant Commissioner's order. Four of these questions disputed the legality of the action of the Assistant Commissioner in first coming to a finding on a point of fact in the interim order and subsequently coming to a different finding in the final order. The remaining questions presupposed that the assessments for the previous years were made on the "accrued" basis from the accounts maintained by the applicant-firm and that as a result of the assessment for 1926-27 having been made on the basis of "cash" receipts, there had been double taxation. This assumption arose from the interim order of the Assistant Commissioner. My predecessor, for the reasons detailed in his order dated the 5th March 1928 (Annexure A), modified the orders of the Assistant Commissioner into an order rejecting the applicant-firm's appeal on the ground that the income for the previous years not having been computed on the accounts of the assessee-firm but estimated in the manner described in paragraph 2 above, the item in question, viz., Rs. 39,000, had not been subject to double taxation. The appellate orders having been modified in this manner, the questions framed by the assessee did not arise and so the application for a reference to the High Court was dismissed (a copy of the Commissioner's order dated the 7th March 1928

is attached—Annexure B) The applicant-firm's objections to the action taken by my predecessor under section 33 to modify the appellate orders are dealt with in this order.

5. The applicant-firm then applied to the High Court under section 66 (3), and in the order of the High Court referred to in paragraph 1, I am directed to state a case. The questions to be referred are stated in two separate judgments appended to the order. In the judgment by Heald, J. the question to be referred is given as follows:—(1) "Whether in a case where an assessment has been made not on actual receipts but on estimated receipts during the previous two years, and the basis of assessment for the third year is changed to a basis on actual receipts, the assessee is entitled to show that the actuals which are taken as the basis of the assessment for the third year, that is, in the present case the year 1926-27, include sums which were included in the estimates for the earlier year or years, on which income-tax was paid for those years?" In the judgment of Otter, J. two questions are formulated. They are as follows:—(2) "Is the applicant-firm entitled to show that the income upon which it was assessed for the three years in question exceeded the income actually received in those three years?" (3) "Can the Commissioner during the pendency of an application to him under sub-sections (2) and (3) of the Income-tax Act (section 66) take up, under section 33 of the Act, proceedings which are the subject of the said application?"

6. As regards the first question the relevant section of the Act is section 13. This section prescribes that in the case of a business the income, profits and gains shall be computed in accordance with the method of accounting regularly employed by the assessee, subject to the following proviso:—"that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine."

Turning to the three assessments in question, the first and second assessments (1924-25 and 1925-26) were made not on the applicant-firm's accounts, but on the basis described in paragraph 2 above, that is, for each of the two years in question the Income-tax Officer without reference to the actual transactions of the year adopted a figure which, in his opinion, was as near an approximation to the firm's income for that year as he could estimate. For the third assessment, he computed the income according to the firm's books. The Income-tax Officer's rejection of the applicant-firm's books in making the first and second assessments cannot now be questioned and it is for the applicant-firm to show that the estimates of its income made by the Income-tax Officer in those two assessments included the disputed amount in the 1926-27 assessment. In attempting to prove its contention the applicant-firm relies on a statement that the two previous assessments were estimates made on the accrued basis. It is true that in the proceedings of the 1925-26 assessment the firm's taxable income is described as having been "worked out in the usual way on the accrued basis method." But this is only a way of describing what is merely a convenient method of estimating the income of a business. The terms "accrued basis" and "cash basis" are properly applicable only where a method of accounting is in question. Here there was no question of a method of accounting since the accounts had not been accepted. The words "accrued basis method" therefore simply indicate the way in which the firm's income was estimated. But after the estimate has been made it is not possible to say that any particular item of receipt or payment is included in it. It is merely the Income-tax Officer's idea of what the firm's income for the year was. If the firm disagrees with it an appeal can be filed (both the previous assessments were appealable) but the firm cannot contend subsequently that a specific item shown in its accounts has been already taxed in the previous assessment. The assessment now in question, that for 1926-

27, was made correctly in accordance with the applicant-firm's method of accounting and since the applicant-firm cannot show that its actual receipts in the accounting year have been already included in the previous year's estimated income, the contention that there has been double taxation fails. In support of these views I refer to the judgment of this Honourable Court in the case *K.T.S.K.A.S. v. Commissioner of Income-tax, Burma*. On this question therefore I am of opinion that the firm is certainly entitled to shew that the 1926-27 assessed income includes income already assessed in previous years but that the firm is unable to show this; that there is no evidence to support the contention that there has been double taxation or in other words that there is evidence on which the Assistant Commissioner and the Commissioner could find as a fact that there has not been double taxation.

7. The second question in so far as it differs from the first should be answered in the negative. The income of the first two years has been finally determined and cannot be questioned now. Only the income of the third year (1926-27) is in question and the firm is entitled only to show that the assessment of this income is excessive or includes actual sums previously assessed.

8. The third question has arisen from the anomalous circumstances in this case in which an Assistant Commissioner in an *interim* order came to a certain finding of fact and when he came to deliver his final order, found that his previous decision was incorrect. When the matter came to the notice of the Commissioner of Income tax through the presentation of an application under section 66 (2) of the Indian Income-tax Act he considered, after much thought, that the question of fact should be decided authoritatively and he invoked his powers under section 33 in order to do so. When the question of fact was definitely settled he found that the basis of the demand for a reference to the High Court had ceased to exist. In my opinion the Commissioner acted within his powers since it is incumbent on him to find the true facts of every case which comes before him. When stating a case to the High Court he must state the true facts and it is essential, therefore, that he should have the power of revising any finding of fact which, in his judgment, is wrong. It is hardly relevant that the finding of fact determined by him may deprive the assessee of the grounds on which he demanded a reference to the High Court on a question of a law. The assessee, however, has still the right to apply to the High Court under section 66 (3) of the Act.

Venkatram, for the Assesseees.

Gaunt, for the Crown.

JUDGMENT

On Civil Miscellaneous Application No. 129 of 1928 the Commissioner of Income-tax was required to state the case of the assessment of the C. T. V. S. Chettyar firm for the year 1926-27 and to refer it to this Court.

His statement of the case shows that for the assessment for the year 1925-26 the firm produced its account books and that after an examination of those books its income was computed at Rs. 19,030 and that for the following year its income was similarly computed to be Rs. 37, 188, the computation for both years being made not according to the income shown in the account books but by a determination of the total capital of the firm and a calculation of the interest which might reasonably be expected to be earned by that capital after deductions in respect of borrowed capital and expenses. For the year 1926-27 a different method of assessment was adopted, the assessment being based on actual receipts of interest in respect of transactions with non-Chettyars, that is, as the Commissioner says, with "the vast majority of the persons to whom loans are made", and on interest accrued due but not necessarily received in respect of transactions with Chettyars. On that basis the assessment for the year 1926-27 was Rs. 36,654. The firm appealed to the Assistant

Commissioner against this assessment on the ground that, so far as transactions with non-Chettyars were concerned, it included actual receipts of interest amounting to Rs. 39,000 which had accrued due in the previous years and according to the method of assessment adopted in those years had been included in the assessment for those years. The Assistant Commissioner accepted that view and sent the case to the Income-tax Officer for a report as to what part of the receipts included in the assessment for 1926-27 represented interest which had accrued in the previous years. The Income-tax Officer reported this sum to be Rs 34,876. The Assistant Commissioner then changed his mind and found that because the assessments for the previous years were not based directly on the firm's accounts, this sum of Rs. 34,876 could not be regarded as having been included in the assessments for those years. He accordingly rejected the claim to have that amount excluded from the assessment. The firm thereupon applied to the Commissioner to refer to this Court certain questions or alleged questions of law. Before disposing of the application for a reference to this Court, the Commissioner reviewed the Assistant Commissioner's orders and substituted for them an order rejecting the appeal to the Assistant Commissioner on the ground that, the assessment for the previous years having been computed on a method of averages, the sum which the firm claimed to exclude from the assessment for 1926-27 had not been subject to double assessment. On the footing of his finding that the basis of the assessment for the two previous years was not technically an assessment on what is known as the "accrued basis" but was "a method of averages", and of his having set aside those parts of the Assistant Commissioner's order which were in question, he held that none of the questions which he was asked to refer arose.

The firm then applied to this Court under the provisions of section 66 (3) of the Act, and a Bench of the Court required the Commissioner to state the case and refer it under that section.

Of the two Judges who dealt with the application under section 66 (3) one was of opinion that the question of law which arose on the facts was whether in a case where the assessment for the two previous years had been made on a basis not of actual income but of income estimated at a certain rate per cent on the capital of the business, and where for the third year the basis of assessment is changed to a basis of actual income, the assessee is entitled to show that the actual income which is taken as the basis of assessment for the third year, includes sums which formed part of the estimated income for the previous years and which had therefore been included in the assessment for those years on which tax had already been paid.

The other learned Judge put the same question in a more practical form, namely: "Is the applicant-firm entitled to show that the income on which he was assessed for the three years in question exceeded the income actually received in these three years?" He also added a question whether during the pendency of an application under section 66 (2) of the Act the Commissioner can exercise his power of review under section 33.

As an answer to the latter question I would say merely that the proviso to section 66 (2) of the Act shows that the Commissioner can exercise that power.

In his order of reference the Commissioner says that "It is for the applicant-firm to show that the estimates of its income made by the Income-tax Officer in those two assessments (for 1924-25 and 1925-26) included the disputed amount." He thus admits the right of an assessee to show that there has been a double assessment, and that right cannot be questioned. If in fact there has been a double assessment it is clear that in law there is no warrant for such double assessment and that income on which tax has already been paid must be excluded from the assessment. But the Commissioner goes on to say that if the assessment for a particular year was based on an estimate and not on actual figures, then the assessee "cannot show" that

income included in a subsequent assessment was included in the assessment based on that estimate. If, as seems probable, this statement was intended to be a statement of fact and to mean that it is impossible to show that income subsequently assessed was included in the computation on which an earlier assessment was based or in the assessment based on that computation, then it is a statement based entirely on the Commissioner's opinion and not on the facts of the case. If on the other hand it was intended to be a statement of the law, namely that where an assessment has been based on a computation under the proviso to section 13 of the Act, an assessee is not entitled to show that income included in a subsequent assessment was included in the computation and in the assessment based on the computation, then it raises a clear question of law which it is for this Court to decide.

As supporting his statement, whether it is a statement of fact or of law, the Commissioner relies on the decision of a Bench of this Court in the case of *K.T.S.K. A.S. Chettyar*, but in that case the Court was clearly of opinion that the inclusion of income in the assessment for one year which had in fact been included in the assessment on which tax had been paid for a previous year would warrant the exclusion of such income from the assessment for the subsequent year, and the basis of the decision was that because the assessment for the previous year was an assessment made by the Income-tax Officer "to the best of his judgment" under section 23 (4) of the Act, and because it was the inclusion of the disputed income in the assessment for that year which was alleged to be mistaken, that alleged mistake could not be allowed to be proved because no appeal lies against an assessment under section 23 (4), so that the applicants, who by their own default had precluded themselves from appealing against the inclusion of that income in the assessment for the previous year, could not in the following year be allowed to claim that the mistake should be corrected by the exclusion of that income from the assessment based on the receipts of the year in which it was actually received. Whether that decision was right or wrong,—and it seems probable that as a general statement of the law it was wrong,—it is no authority for the proposition that where income has been assessed for one year under the proviso to section 13 [and not under section 23 (4)] the assessee cannot, whether in fact or in law, show that the income has been included in the assessment for the following year.

A case which was in some respects similar to the present case was decided by a special Bench of the High Court of Madras in the *Commissioner of Income-tax v. Mutha Sarvarayudu* (1), where the question referred was "Where computation of the income, profits and gains for a particular year is made as directed in the proviso to section 13 of the Income-tax Act of 1922, are any income, profits or gains which accrued during that year but are received subsequently liable to be assessed as income for the year during which they are received?" The Bench said that if the wording of the question was intended to propound the question whether, if a man has been taxed in respect of book debts owing to him in one year which he has not actually received, he can again be taxed on the same sums of money when they are actually received in cash in a later year of assessment, the answer must obviously be "No." But in that particular case the Commissioner had recorded, as a finding of fact based on the evidence in the case, that the sums which the assessee claimed to deduct from his assessment for the subsequent year had not been included in the assessment for the previous years, and by reason of that finding the learned Judges said that the question referred could not really arise out of the findings of fact, which were binding on them, namely that the man had not been taxed at all on the sums in question until he was sought to be taxed in the year of assessment which was under consideration in that case.

In the present case there is no finding of fact that the sums in question were not included in the assessments for the previous years. On the contrary the only finding

of fact on this subject is that of the Income-tax Officer that Rs. 34,876 had been so included. The findings on the footing of which the Assistant Commissioner and the Commissioner rejected the claim were either findings of fact based on no evidence, or findings of law, since they were that the assessee could not prove that the sums in question were included in the "computation" which was made under the proviso to section 13. The Commissioner said that his finding on this point was a finding of fact, and he put into the form of a finding of fact when he said that there had not been a double assessment, but the reason which he gave for that finding, namely that the assessments for the previous years had been computed on a method of averages, and that the assessee could not prove that the disputed income had been included in those assessments shows that his answer begged the question of law and as a finding of fact was not based on any relevant evidence.

The facts of the case are that the assessments for 1924-25 and 1925-26 were based on a computation of income, profits and gains under the proviso to section 13 of the Act, that that computation was made by reckoning interest at a certain rate per cent on capital; that that computation included all interest earned or "accrued" whether it had been received or not; that for the year 1926-27, so far as interest from non-Chettyar customers was concerned, the basis of the assessment was changed from a basis of computation of accrued interest to a basis of interest actually received; that by reason of that change the question arose whether interest actually received in the year, on the income of which the assessment for 1926-27 was based had accrued and had therefore been included in the computation and assessments for the previous years; and that the Income-tax Officer found that a sum of Rs. 34,876, which was received in the year on the income of which the assessment for 1926-27, was based and was therefore included in the assessment for 1926-27 had in fact accrued and had therefore been taxed in the previous years.

On these facts it seems clear that there had been a double assessment and that the assessee was entitled to relief unless the Commissioner was right in holding that because the assessments for 1924-25 and 1925-26 were made under the proviso to section 13, the assessee could not prove that income included in the assessment for 1926-27 was based and was therefore included in assessment for 1926-27, had already been included in the assessments for 1924-25 and 1925-26.

I know of no authority in the Act or elsewhere for the view that the fact that the basis of an assessment was a computation under section 13 of the Act precludes the assessee from showing that particular income was included in that assessment, and I see no reason to believe that there is in fact any warrant for the Commissioner's opinion that it is impossible for an assessee to show that such income was included in such an assessment.

I would accordingly decide the question, which in my opinion is raised by the case, by saying that where the computation of income, profits and gains for a particular year has been made under the proviso to section 13 of the Act "upon such basis and in such manner as the Income-tax Officer may determine," the assessee is entitled to show that income, profits or gains included in the assessment for a subsequent year were included in that computation, and that it is a question of fact, to be decided on the evidence in the particular case, whether he succeeds in showing that they were so included.

I would direct the Commissioner to pay the costs of the firm in this reference and in Civil Miscellaneous Application No. 129 of 1928, advocate's fee in each case to be ten gold mohurs.

(328) IN THE COURT OF THE JUDICIAL COMMISSIONER AT NAGPUR

Before Mr. Macnair, Offg. Judicial Commissioner and Mr. Jackson, Additional
Judicial Commissioner

(14th August, 1929)

Ramakrishna Ramnath Firm of Tirora Assessses.

vs.

The Commissioner of Income-tax, Central Provinces and
Berar Referring
Officer.

*Indian Income-tax Act Act (XI of 1922), Secs. 5 (4). 10 (2) (ix) and 66 (3)—
Central Provinces Gazette Notification No. 97—Income-tax Officer's Jurisdiction over
assesseees assessed to Rs. 40,000—Failure to object, effect of—Sums paid to partner,
when deductible from firm's assessable income—Jurisdiction to question order calling
for reference.*

*The Court hearing a reference under the Income-tax Act has no jurisdiction to
question the validity of the order of the Court under section 66 (3) directing the
Commissioner to state a case passed after hearing the Commissioner.*

*The jurisdiction of an Income-tax Officer over assesseees who were at any time
assessed to Rs. 40,000 is taken away by Central Provinces Gazette Notification No.
97 dated 28th March, 1923 and consequently any notice under section 22 (2) issued by
an Income-tax Officer in such cases though not objected to, is illegal.*

*Remuneration paid to a partner doing business in his individual capacity for
services rendered to the firm would be a legitimate deduction from the assessable in-
come of the firm ; but sums paid to a partner as such styled commission, pagdi (bonus
or present) or by any other name would be simply the profits of the firm appropriated
among the owners after they had been earned.*

Case [Miscellaneous Judicial Case No. 32 of 1927] stated under Sec. 66 (3) of
the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax,
Central Provinces and Berar, for the opinion of the Court.

CASE

By order of the High Court dated the 16th February 1929, I have been directed
under section 66 (3) of the Indian Income-tax Act (XI of 1922) to refer to them the
following questions of law arising out of the assessment to income-tax for the year
1925-26 of the unregistered firm of Ramakrishna Ramnath, owners of a Bidi
(Cigarette) factory at Tirora :—

- (i) Whether in view of the C. P. Gazette Notification No. 97, dated the
28th March 1923 by the Commissioner of Income-tax, the Income-tax
Officer's jurisdiction, in cases of assesseees who were at any time assess-
ed to Rs. 40,000 and above since 1919-20 is taken away and if so,
whether the notice under section 22 (2) issued by him is legal.
- (ii) Whether the Assistant Commissioner of Income-tax is empowered under
any of the provisions of the Income-tax Act to delegate his powers of
issue of notices under section 22 (2) to the Income-tax Officer in
general or in special cases and if so, whether that authorisation can
have any retrospective effect.

- (iii) Whether the words "the case is now fixed for 27th July 1925 when necessary action will be taken if default further continues" in the warning notice issued by the Income-tax Officer precluded extension of time for filing a return under section 22 (2).
- (iv) Whether the return so filed before 27th July 1925 could not be deemed to be a proper return under section 22 (2).
- (v) Whether the commission for sale of Bidis manufactured in partnership is allowable to a partner under section 10 (2) (ix) of the Act when the expenditure so incurred is solely for earning the profits of the business, when the same is paid as per registered deed of the agreement of partnership, when the partner who so sells Bidis has to maintain a separate establishment for this purpose and specially for the reason that the sale of Bidis is retail and that such sale is not in the usual course of business of the firm and that agencies for such sale are usually given to others in other places.
- (vi) In the same way whether *Pagdi* money which is in the nature of bonus is allowable under section 10 (2) (ix).
- (vii) Whether *Goushala* levy and *Rashtriya* fund levy on sales of Bidis effected and charged to the account of the above two funds can be held to be the income of the assessee under any section of the Income-tax Act.

2. The assesseees have since expressed a regret before me on 6th April, 1927, withdrawing their application for a reference in respect of question (vii). I shall therefore confine myself to the remaining six questions.

3. The facts of the case are as follows :—The Income-tax Officer, Bhandara, served on the applicants on 13th April 1924, a notice under section 22 (2) of the Indian Income-tax Act calling on them to furnish in the prescribed form on or before May 13th, 1924, a return of their income for the year ending with "Diwali" in the calendar year 1924. The return was not filed by the due date. One of the partners appeared before the Income-tax Officer on 9—5—25 and asked for the time for filing the return might be extended.

4. Time was accordingly allowed up to 26—6—25, but no return was received by that date. The case was adjourned to 4—7—25 but still no return was received. On that date the Income-tax Officer recorded the following order :—"No return yet. Partner Minhajuddin Khan who met me at Tumsar railway station on the 24th June had promised to file return at Bhandara on due date but has made a default. Issue reminder and threaten very heavy *ex parte* assessment. Case for 27—7—25." On 10th July, 1925, a special agent of the firm filed before the Income-tax Officer an application for the registration of the firm under section 14 (2) of the Indian Income-tax Act.

5. For reasons that will appear later the Income-tax Officer submitted this for orders to the Assistant Commissioner who after hearing the applicants on 25th July 1925, rejected the application by his order dated 26th August 1925. Against this order the applicants presented a petition to the Commissioner of Income-tax (my predecessor, Mr. Kekre) requesting him to revise under section 33 the order of the Assistant Commissioner refusing registration. This petition was rejected by the Commissioner of Income-tax in his order dated 11th January 1926.

6. Meanwhile, on 27th July 1925, the applicants had submitted a return under section 22 (2) declaring an income of Rs. 69,656 which they afterwards

corrected to Rs. 73,857. They produced their accounts before the Income-tax Officer who examined them and submitted a report to the Assistant Commissioner recommending assessment on Rs. 1,00,415.

7. I must now explain that Commissioner of Income-tax by his notification No. 97/98, dated 28-3-23 (Copy App. A) had directed under section 5 (4) of the Indian Income-tax Act that the Assistant Commissioner should exercise the powers of Income-tax Officer (and the Commissioner of Income tax those of Assistant Commissioner) in respect of all assessee whose income amounted to Rs. 40,000 or more. The Assistant Commissioner was therefore the Income-tax Officer for the purpose of the case under consideration.

8. The Assistant Commissioner heard the assessee on 25th November 1925, and on the following day passed an order assessing them on a total income of Rs. 93,890.

9. Against this order an appeal under section 32 of the Indian Income-tax Act was filed before my predecessor (acting as Assistant Commissioner) on 23rd December, 1925, on the following grounds:—(1) The Assistant Commissioner should not have refused to register the firm, (2) he should not have disallowed:—(a) Rs. 6,500 paid as commission to Abdulla Mohamed of Akola (one of the partners of the assessee firm), (b) Rs. 1,000 "pagdi" expenses paid to the same partner, (c) Rs. 6,627-12-9 expenses of the Akola agency for which no accounts were produced, and (d) certain sums credited to Rastriya and Goushala.

10. By his order dated 26th January 1926 my predecessor allowed a sum of Rs. 5,307 on account of the expenses of the Akola agency and in respect of the other grounds rejected the appeal. (So far as the first ground is concerned, I may remark that the Act does not provide for any appeal against an Income-tax Officer's order refusing to register a firm). The total income was thus reduced to Rs. 88,583.

11. On the 24th February, 1926, the assessee presented an application for a reference to the High Court on the points already mentioned. My predecessor by his order dated 16th March, 1926 rejected the application.

12. Subsequently the assessee presented an application to the High Court under section 66 (3) and as already stated the High Court directed me to make this reference.

13. I will now state my opinion as required by section 66 (2) on the questions referred to the High Court. In the first place, I beg to point out that an application under section 66 (3) can only be made when a reference has been refused under section 66 (2). An application for a reference under section 66 (2) can only be made in respect of questions of law arising out of an order under sections 31 or 32. Consequently I submit that the High Court acting under section 66 (3) can only direct that a reference be made to it in respect of questions of law arising out of an order under section 31 or section 32.

14. Questions I to IV above do not arise out of an order under section 31 or section 32. They relate (1) to the validity of the notice under section 22 (2) issued by the Income-tax Officer, Bhandara and (2) to the validity of the order refusing registration.

15. The first of these questions was not raised in appeal and therefore in the appellate order under section 31 it was not dealt with and it cannot be said to be a question arising out of an order under section 31.

16. The second of these questions was, it is true, raised in appeal but as I have already pointed out no appeal lies under section 30 against an order of an

Income-tax Officer refusing registration. The Commissioner acting as Assistant Commissioner in his appellate order did not deal with this question beyond mentioning that he had already disposed of it in his order under section 33. Under section 31 he had no power to deal with this question. This question also therefore does not arise out of an order under section 31. I therefore beg to refer to the Honourable Court under section 66 (1) the preliminary question:—Whether this High Court has any jurisdiction to decide questions I to IV above? And as required by law I deferentially express my own opinion which is that the High Court has no such jurisdiction.

17. In the circumstances it seems sufficient to state briefly that I consider that there was no material irregularity in regard to the issue of the notice under section 22 (2) in this case. The applicants had themselves applied on the 10th July 1925 to the Income-tax Officer, Bhandara, for registration of their firm. This application was sent up as required by law for orders of the Assistant Commissioner and when on the 17th July 1925 the Assistant Commissioner asked the applicants to show cause why the application should not be rejected as time barred, then only did the applicants raise the question of the jurisdiction of the Income-tax Officer. They had accepted the notice under section 22 (2) issued by the Income-tax Officer, Bhandara and had even applied more than once to him for the extension of the time to file the return under section 22 (2) as he has shown above. They are therefore estopped from raising any question of law in regard to it now both by the provisions of the Indian Income-tax Act and by the ordinary law of estoppel (Questions i and ii). I consider that the order refusing the registration was proper (Question iii) inasmuch as the application for registration was not in time as required by Rule 2 of the Rules under the Income-tax Act, *vide Purushottam Bhanji & Co. v. Commissioner of Income-tax, Bombay* (1). Section 22 (2) does not, as a matter of fact, empower the Income-tax Officer (as section 22 (1) does) to extend the time for submission of a return when once it has been fixed. This answers question (iv).

19. It only remains to deal with questions V and VI. *Question V* as framed is not very lucid. It is clear that if a partner of a firm as such conducts business on behalf of the firm any remuneration, whether styled commission or by any other name, paid to him as such partner by the firm for carrying on the business of the firm whether in accordance with the terms of the deed of partnership or otherwise is simply part of the profits of the firm distributed in a particular manner. I need only refer to the decision of the High Court of Madras in *Chief Commissioner of Income-tax (Board of Revenue), Madras v. Vegaraju Venkatasubbaya Garu* (2). Their Lordships said very briefly. "We have no hesitation in answering that the drawings of the partners by whatever name they are described are part of the profits and therefore taxable". In that case the drawings were called "Salary". Here they are called commission.

20. The question is really a question of fact. No doubt the partner in question has a legal personality apart from that of the firm. He might conceivably do business in his individual capacity and in that capacity might render services to the firm in consideration of which the firm might pay him a remuneration which would be a legitimate deduction from the assessable income of the firm. But obviously, considering the opportunities for fraud that any such alleged arrangement would offer, very strict proof would reasonably be required of the existence of such an arrangement, and as a matter of fact no attempt has been made to prove that such an arrangement exists in the present case. On the contrary the terms of the partnership deed show that the payment was made to the partner, as partner, for conducting the partnership business.

Question VI. The payments of *pagdi* (bonus or present) are on precisely the same footing. If anything, the position of the Department in regard to them is

stronger. They are purely and simply distributions of profits. If such payments to partners were allowed as a charge against the assessable profits of firms obviously no firm need ever pay income-tax at all. They are not payments made in order to earn profits, but appropriations of profits among the owners of such profits after the profits have been earned.

APPENDIX A

NOTIFICATION

Dated Nagpur the 28-3-1923.

No. 97/98. In pursuance of sub-section (4) of section 5 of the Indian Income-tax Act, 1922), (as applied to Berar) the Commissioner of Income-tax, Central Provinces and Berar hereby directs that until further orders in all cases where the total assessable income was Rs. 40,000 and above in any year since 1919-20 the powers of the Income-tax Officer shall be exercised by the Assistant Commissioner and those of the Assistant Commissioner by the Commissioner of Income-tax.

1—4—22

C. P. Gazette Notification No. 4/9 dated the——— is hereby cancelled.

5—5—22

(Sd.) K. S. JATAR.

Commissioner of Income-tax,

Central Provinces and Berar.

R. N. Padhey, for the Assesseees.

D. N. Choudhri, for the Crown.

JUDGMENT

(1) The Income-tax Officer, Bhandara, served on the non-applicants on 13th April 1925 a notice under section 22 (2) of the Income-tax Act calling on them to furnish in the prescribed form on or before May 13th, 1925, a return of their income for the year ending with the Diwali in the calendar year 1924. The time for filing this return was extended by the Income-tax Officer up to the 26th June 1925. On 10th July 1925 an application was made to the Income-tax Officer for the registration of the firm under section 14 (2) of the Income-tax Act; this application was considered by the Assistant Commissioner and was rejected on the ground that it was not made in time. An application for revision of this order was made to the Commissioner of Income-tax but was rejected.

(2) The non-applicants submitted a return under section 22 (2) of the Income-tax Act and an assessment order was passed by the Assistant Commissioner; an appeal to the Commissioner of the Income-tax was filed but was successful only to a small extent. The assesseees then presented an application for a reference to the High Court on the following points:—

(i) Whether in view of the C. P. Gazette Notification No. 97, dated the 28th March 1923, by the Commissioner of Income-tax, the Income-tax Officer's jurisdiction in cases of assesseees who were at any time assessed to Rs. 40,000 and above since 1919-20 is taken away and if so whether the notice under section 22 (2) issued by him is legal.

(ii) Whether the Assistant Commissioner of Income-tax is empowered under any of the provisions of the Income-tax Act to delegate his powers of issue of notices under section 22 (2) to the Income-tax Officer in

general or in special cases and if so whether that authorization can have any retrospective effect.

- (iii) Whether the words 'the case is now fixed for 27th July 1925, when necessary action will be taken if default further continues' in the warning notice issued by the Income-tax Officer precluded extension of time for filing a return under section 22 (2).
- (iv) Whether the return so filed before 27th July 1925 could not be deemed to be a proper return under section 22 (2).
- (v) Whether the commission for sale of Bidis manufactured in partnership is allowable to a partner under section 10 (2) (ix) of the Act when the expenditure so incurred is solely for earning the profits of the business, when the same is paid as per the registered deed of the agreement of partnership, when the partner who so sells Bidis has to maintain a separate establishment for this purpose and specially for the reason that the sale of Bidis is retail and that such sale is not in the usual course of business of the firm and that agencies for such sale are usually given to others in other places.
- (vi) In the same way whether *Pagdi* money which is in the nature of bonus is allowable under section 10 (2) (ix).
- (vii) Whether *Goushala* levy and *Rashtriya* fund levy on sales of Bidis effected and charged to the account of the above two funds can be held to be the income of the assessee under any section of the Income-tax Act.

This application was rejected: the assessee applied to the High Court under section 66 (3) of the Income-tax Act and Mr. Kinkhede, Additional Judicial Commissioner, after hearing Counsel on both sides, stated that he was not satisfied of the correctness of the Commissioner's decision on the points on which reference was sought and required the Commissioner to state the case to this Court. The assessee does not desire reference on the 7th point and the Commissioner has referred to the High Court the first six questions.

(3) Rai Bahadur D. N. Chowdhari urges a preliminary objection that no question of law arises out of the order passed by the Commissioner of Income-tax in an appeal under the provisions of section 32 of the Income-tax Act: his main contention is that in that order the correctness of the refusal to register the firm was not considered. But this Court after hearing both sides directed the Commissioner to state and refer the case. We consider that we have no jurisdiction to decide a point which has already been decided after a full hearing by this Court. If authority for this proposition is needed, we may refer to *Trikamji Jiwan Das v. Commissioner of Income-tax, Bihar and Orissa* (1). The Counsel for the Commissioner of Income-tax refers us to *P. Thiruvengada Mudaliar v. Commissioner of Income-tax, Madras* (2) but in that case the Commissioner had not been given an opportunity to oppose the application that he should state a case and the Court was clearly competent to revise an order passed behind the back of one of the parties. We doubt the correctness of the order of this Court but cannot now question its validity.

(4) The first four questions as stated before us refer to the correctness of the refusal to register the firm. The Income-tax Officer, Bhandara, and the Assistant Commissioner of Income-tax obtained jurisdiction to assess income-tax from the provisions of section 5, clause (4) of the Act: this is as follows:—
 "Assistant Commissioners of Income-tax and Income-tax Officers shall, subject to the control of the Governor-General in Council, be appointed by the Commissioner

of Income-tax by order in writing. They shall perform their functions in respect of such classes of persons and such classes of income and in respect of such areas as the Commissioner of Income-tax may direct. The Commissioner may, by general or special order in writing, direct that the powers conferred on the Income-tax Officer and the Assistant Commissioner by or under this Act shall, in respect of any specified case or class of cases, be exercised by the Assistant Commissioner and the Commissioner respectively, and, for the purposes of any case in respect of which such order applies, references in this Act or in any rules made hereunder to the Income-tax Officer and the Assistant Commissioner shall be deemed to be references to the Assistant Commissioner and the Commissioner, respectively." It is not disputed that by C. P. Gazette Notification No. 97/98, dated the 28th March 1923, it was directed that the powers conferred on the Income-tax Officer and the Assistant Commissioner under the Act should be exercised in respect of the class of cases to which the case of the assessee belongs by the Assistant Commissioner and Commissioner of Income-tax respectively. Section 22 (2) which directs the Income-tax Officer to serve a notice upon the assessee must then be read as if the Assistant Commissioner was so directed. The Income-tax Officer, Bhandara, then had no authority to serve a notice on the assessee. We answer the first part of the question No. 1 in the affirmative.

(5) It is urged on behalf of the Commissioner that the Income-tax Officer may have acted on behalf of the Assistant Commissioner. The notice does not show that he so acted and the Commissioner when stating the case does not suggest that this is so. It is next urged that the assessee who accepted the notice from the Income-tax Officer and applied for extension of time waived the right to object to the jurisdiction of the Income-tax Officer; no action of the assessee can give the Income-tax Officer jurisdiction that the law does not give him. The answer to the second part of question 1 is that the notice was illegal.

(6) The second question is couched in general terms and has not been argued before us. It appears that an opinion on this question is not now desired.

(7) On the third question it is sufficient to state that the words quoted indicate that default has occurred. The notice then does not vary the date on which the return was due. But this is immaterial as our answer to the next question raised before us must be that the notice did not make the return due. That question was not exactly question No. 4: what was urged was that the application for registration of the firm, in order to make applicable provisions of the Act relating to a registered firm as defined in section 2 (14) of the Act, was made within the period allowed by law. The rule then in force was rule 2 of Income-tax Rules of 1922, which is as follows:—"Any firm constituted under an instrument of partnership specifying the individual shares of the partners may, for the purposes of clause (14) section 2 of the Income-tax Act, 1922 (hereinafter in these rules referred to as the Act), register with the Income-tax Officer the particulars contained in the said instrument on application in this behalf made by the partners or by any of them on or before the date on which a return is due under sub-section (2) of section 22 of the Act." We are of opinion that as the notice issued by the Income-tax Officer was illegal, it did not cause the return, to which sub-section (2) of section 22 refers, to become due. Our answer to the question argued is that the application for registration was within time.

(8) There does not seem to be any dispute on any question of law raised in questions 5 and 6. As the Commissioner of Income-tax remarks: "A partner might conceivably do business in his individual capacity and in that capacity might render services to the firm in consideration of which the firm might pay him a remuneration which would be a legitimate deduction from the assessable income of the firm." But even if the terms of the partnership deed indicated that one partner was so to do business, the Commissioner is not bound to hold that this is the case:

a statement in the partnership deed may be intended to assist escape from the provisions of the Income-tax Act. We cannot interfere with the decision of fact that the assessee has not proved that the arrangement to which the Commissioner refers really existed. The only answer which we can give to questions 5 and 6 is the statement of the law made by the Commissioner of Income-tax.

(9) In order to avoid misapprehension it is necessary to add that our decision of the questions raised does not necessarily affect the assessment of income-tax with which the order of the Commissioner dealt. The assessee was not a registered firm, even if their application for registration was wrongly considered to be barred by time.

The cost of this reference will be borne as incurred.

(329) IN THE COURT OF THE JUDICIAL COMMISSIONER AT NAGPUR

*Before Mr. Macnair, Offg. Judicial Commissioner and Mr. Jackson,
Additional Judicial Commissioner*

(13th August 1929)

Kikabhai and others Assessee.*

vs.

The Commissioner of Income-tax, Central Provinces and Berar. Referring
Officer.

Indian Income-tax Act (XI of 1922) Sec. 2 (14)—Assessee living together and carrying on business under partnership agreement—Profits not divided but left in business—Assessability as a registered firm.

The assessee, three brothers living, messing and carrying on their ancestral business jointly, executed a partnership deed providing for the profits and loss to be shared by them equally. No accounts of the income nor separate ledgers in their names were kept and the profits of the business after drawings of fixed sums for personal expenses of each of the brothers and for common household expenses were left in the business. The assessee's application for registration of the firm was refused on the ground that as the brothers had no intention then or in future to divide or credit the profits, the prescribed certificate as to division of profits submitted by them was incorrect. On a reference to the High Court,

Held, that the certificate having been given in good faith the assessee constituted a firm entitled to be registered under Sec. 2 (14) of the Income-tax Act.

Case [Miscellaneous Judicial Case No. 58 of 1928] stated under Sec. 66 (1) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the Court.

CASE

Under section 66(1) of the Income-tax Act, I beg to refer the following point of law for the decision of the Honourable Judges of the High Court:—"Whether the three Shia Bohra brothers of Raipur, i.e., Kikabhai, Ibrahimji and Taherbhai, who

have inherited the property and business of their father Abdulali, who are living, messing and carrying on business jointly, who keep no accounts of the income made during the year, who keep no separate ledgers in their books of accounts for themselves, who have no intention to do so in future and who have no intention to divide their profits, could be declared 'a registered firm' under section 2 (14) of the Income-tax Act".

Facts of the Case.—The facts of the case are as follows:—Abdulali, a Shia Bohra of Raipur, was doing business under the name and style of A. Ahmadjibhai. He died about 12 years ago leaving his widow and three sons, Kikabhai, Ibrahimji and Taberbhai, behind him. They all live together and the business is continued under the old name and has been assessed in the past under different names such as "A. Ahmadji Bahi", "Seth A. Ahmadji Bhai & Co.", "A. Ahmadji Bahi & Co., owners Kikabhai and Brothers", "A. Ahmadji Bhai & Co." Thus there has been no uniformity of the name under which these men have been assessed in the past. In the letter heads, correspondence, hand bills, etc., the name of the business is shown as "A. Ahmadji Bhoj, General Merchant, Raipur" and sometimes as "A. Ahmadjibhai" only.

3. The three brothers applied to the Income-tax Authorities for being registered as a registered firm. Their application was refused by the Income-tax Officer and on appeal against that order, the Assistant Commissioner also refused to register the firm. The application of the brothers for a reference to the High Court has been rejected by me since there was no valid order under section 30, but as the question raised is of general importance, I have ventured to submit this reference under section 66 (1).

4. When Abdulali died he left behind him his widow and three sons but no daughter. There has been no separation or partition among them and they are carrying on the business jointly. The mother is said to have waived her right in the estate of the deceased in favour of the three sons and is being maintained by them jointly. The accounts of the receipts and expenditure are kept jointly in the name of the shop. No account is made up to find out the annual profits, nor have the profits been ever apportioned up till now. It is not the intention of the brothers to partition their income or even to enter it in the books of accounts separately. There is no ledger (Khata) of the three brothers in the books of accounts. They have stated that they do not intend to credit the profits of the year 1927-28 or even of any subsequent years to their personal ledgers. Their practice is to draw Rs. 530 per mensem from the shop for household expenses. Of this amount each brother takes Rs. 50 for his pocket expenses and the remainder is given to the mother who keeps Rs. 80 for her private expenses and spends Rs. 300 for messing expenses of the whole family. No accounts are called for from the mother as regards the expenditure of Rs. 300. Rs. 50 taken by each of the three brothers is spent on their clothes and other requirements. If any brother requires anything more than this in any month that is given to him and only then a ledger account is opened for this and he has to return this amount out of the saving of the Rs. 50 his monthly allotment.

5. *Opinion.*—To get themselves declared "a registered firm" the three brothers executed a deed of partnership on the 5th of July 1927, copy enclosed (Ex. A) and put up an application for registration in the form prescribed by Rule 3 of the Income-tax Rules, 1922. This application too was presented on the 5th of July 1927; but the Income-tax Officer, as stated above, refused registration.

6. Under the Income-tax Act, a partnership which has been registered by the Income-tax Officer and declared a registered firm, gets favourable treatment; that is to say, though the firm itself is taxed at the maximum rate, its partners can apply for the refund of the tax paid on their shares and can get taxed separately on their total

income at the rate applicable to them. A registered firm means "a firm constituted under an instrument of partnership specifying the individual shares of the partners of which the prescribed particulars have been registered with the Income-tax Officer in the prescribed manner." Under section 239 of the Indian Contract Act a partnership is defined as "the relation which subsists between persons who have agreed to combine their property, labour or skill in some business, and to share the profits thereof between them" and "Persons who have entered into partnership with one another are called collectively a 'firm'." Thus before an association of individuals can be registered as a registered firm under section 2 (14) of the Income-tax Act, the association shall be a firm satisfying the conditions laid down in section 239 of the Indian Contract Act. The question is whether this Bohra family is a firm (*i.e.*, a partnership) or co-ownership. They are not a joint Hindu family though like so many other Bohras they live in joint family system and claim to be governed under the Shia branch of the Mohammadan law. They have inherited the property and the business from their father and though they may be supposed to have agreed to combine their property, labour, and skill in that business, they have no intention to share the profits thereof between them. They state: "We do not intend to partition our profits or write them in our separate ledgers so long as we are living and pulling on together. We shall separate our whole estate including our profits when we separate ourselves and not till then". This statement clearly shows that the partnership deed is by brothers' own admission not a genuine partnership deed but one prepared *ad hoc* simply to secure favourable treatment under the Income-tax Act. It contains false recitals at variance with the true intentions of the parties. The intention to share the profits which is a necessary incident of partnership is wanting and this combination of the three brothers cannot therefore be called a partnership and the persons cannot be called collectively a firm.

7. Moreover, taking for argument's sake that the three brothers constituted a firm as defined under section 239 of the Contract Act, they do not still fulfil the requirements of the Income-tax Act under which a firm is to be registered. In paragraph 8 of the form of application prescribed in Rule 3 of the Income-tax Rules, 1922, it is necessary for the applicant-firm to certify as: "We do hereby certify that the profits of the year ending in. . . . will be actually divided or credited in accordance with the shares shown in this partnership deed". Therefore, even though it were conceded that the three brothers formed a firm within the meaning of the Indian Contract Act, it would still be not possible to register the firm so long as the partners had no intention to divide the profits or credit them in accordance with the shares shown in the partnership deed.

8. I am therefore of opinion that this association of individuals is not entitled to be declared a registered firm under the Income-tax Act and I submit that the answer to the question under reference should be in the negative.

EXHIBIT A

Deed of partnership executed by:—(1) Kikabhai S/O Abdulali, aged about 48 years, (2) Ibrahimbhai S/O Abdulali, aged about 41 years, (3) Taherbhai S/O Abdulali aged about 36 years, Whereas we the above mentioned three persons were carrying on business of Manihari, Stationery, General merchandise, Timber and other goods in partnership since long under the name and style of A. Ahmadjibhai at Raipur and Rajnandgaon but had no legal writing till now to show the existence of a partnership and the extent of the shares held by each of us. We, therefore, hereby now declare that since Kartik Sudi 1 Samvat 1982 corresponding to 18th October 1925 we the above named three persons constitute partners in the Firm styled as "A. Ahmadjibhai" of Raipur and that each one of us holds 0-5-4

share in the Firm and that each one of us is entitled to the profits and is bound to contribute towards the losses of the business as the case may be, in equal shares.

M. B. Niyogi, for the Assesseees.

D. N. Choudhari, for the Crown.

ORDER

Under section 66 (1) of the Income-tax Act the Commissioner of Income-tax has submitted the following point of law for decision:—"Whether the three Shia Bohra brothers of Raipur, *i.e.*, Kikabhai, Ibrahimji and Taberbhai, who have inherited the property and business of their father Abdulali, who are living, messing and carrying on business jointly, who keep no accounts of the income made during the year, who keep no separate ledgers in their books of accounts for themselves, who have no intention to do so in future and who have no intention to divide their profits, could be declared 'a registered firm' under section 2 (14) of the Income-tax Act."

2. The three brothers do business under the name of A. Amadjibhai. They live together with their mother and each month Rs. 530 is withdrawn from the shop, of which each of the brothers takes Rs. 50 for personal expenses and Rs. 300 for household expenses. The rest of the profits are left in the business. It seems to us that the three brothers can be held to constitute a firm within the meaning of section 239 of the Contract Act, because they do intend eventually to share among them the profits of the shop. The definition of "partnership" in that section does not require the profits to be shared at any particular time. Partners can leave their profits in the business, and the real test is whether each could withdraw his share; if he so desired. In the present case, it would appear that the arrangement between the brothers is such that one of them could not withdraw only his share of the profits; but each could withdraw from the business and demand his share of the assets including the accumulated profits.

3. The Commissioner of Income-tax contends, however, that not every firm is entitled to be registered under section 2 (14) of the Income-tax Act. A firm desiring registration must furnish prescribed particulars in the prescribed manner to the Income-tax Officer. In the form prescribed in the Indian Income-tax Rules a certificate has to be given that the profits for the year last ended have been or will be actually divided or credited in accordance with the shares shown in the partnership deed. In the present case, the certificate given is that the profits of the year ending Diwali 1926 will be actually divided or credited. The certificate is in order, but the Commissioner alleges that it is incorrect, because the brothers have no intention to divide or credit the profits. The certificate to be given is not that the profits will be divided or credited within some fixed period; and it seems to us that, when a certificate in the prescribed form is given in good faith, if the applicants do constitute a firm, that firm is entitled to be registered.

4. In the present case we are satisfied that the certificate was given in good faith. There is no doubt as to the facts. The brothers have each got a one-third share in the shop that they own and that is not denied. They intend to divide the assets whenever it may be necessary or convenient for them to do so, and on the division being made, each will necessarily get a share of the profits made during each and every year that they carried on business in partnership.

5. We consider that the three brothers carrying on business under the name of A. Amadjibhai are entitled to become a registered firm under section 2 (14) of the Indian Income-tax Act.

(330) IN THE HIGH COURT OF JUDICATURE AT RANGOON

Before Sir Benjamin Heald, Kt., Off. Chief Justice, Mr. Justice
P. N. Chari and Mr. Justice Ormiston.

(29th August, 1929).

S. P. K. A. A. M. Chettiyar Firm Assesseees.

vs.

The Commissioner of Income-tax, Burma Referring
Officer.

Indian Income-tax Act (XI of 1922), Sec. 23 (4)—Arbitrary assessment—Reasons and basis therefor to be stated—Scope and limits of Income-tax Officer's powers.

An entirely arbitrary assessment under Sec. 23 (4) of the Income-tax Act without giving any reasons or indication of its basis beyond the Income-tax Officer's private opinion is illegal. An assessment under section 23 (4) though necessarily to some extent arbitrary must be reasonable and the materials or the reasons on which it is founded must be so stated that the Commissioner may be in a position to ascertain whether or not it is reasonable.

Case [Civil Reference No. 10 of 1929] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

CASE

In accordance with the High Court's order dated the 18th March 1929 in Civil Miscellaneous Application No. 135 of 1928, the following question arising out of the assessment of the S. P. K. A. A. M. Chettiyar firm of Rangoon for the year 1927—28 is stated for the decision of the High Court, under the provisions of section 66 (3) of the Income-tax Act:—"Whether the Income-tax Authorities acted legally in assessing the applicant under section 23 (4)?"

2. The Income-tax Officer is required to make the assessment under section 23 (4) whenever the person to be assessed fails to produce all the accounts called for on a notice issued under section 22 (4). In the present case the Income-tax Officer held that the applicant did not comply with all the terms of the notice under section 22 (4) and this finding of fact was upheld by the Assistant Commissioner on appeal. The only point to be considered therefore is whether there was evidence on which the Income-tax Officer and the Assistant Commissioner could have come to this finding of fact.

3. The facts of the case material to the question at issue are as follows:—

The applicant-firm made a return of income under section 22 (2). By a notice under section 22 (4) the firm was required to produce all the accounts and documents of its business for the Tamil year "Akshaya" (13th April 1926 to 12th April 1927). Certain books of account were produced but the Income-tax Officer noticed that these accounts did not show items of receipt corresponding to two items of payment of interest which had been made to the firm by two other firms during the accounting year. A sum of Rs. 487-1-9 was paid by a Chettiyar concern at Wakema and another sum of Rs. 1,801-9-6 by a non-Chettiyar concern at Kayan. No satisfactory explanation was given by the applicant-firm in regard to

these omissions and further enquiries by the Income-tax Officer elicited the following facts, namely :—(a) that a Chettyar firm (M.M. Wakema) received three loans from the applicant-firm during the period 13th August 1925 to 13th August 1926 of which one was not recorded in the books of the S.P.K.A.A.M. firm ; (b) that a non-Chettyar firm (K.S.M. Kayan) received twenty loans during the accounting year 1926-27 from the applicant-firm of which five were not recorded in the books of the S.P.K.A.A.M. firm.

The explanations given by the applicant-firm in regard to these missing loans are discussed in the Income-tax Officer's order marked " A. " * Briefly, they were to the effect that the loans in question were made by one of the partners of the firm and not by the applicant-firm. These explanations were not supported by any documentary evidence and they were also so inconsistent and improbable that the Income-tax Officer was forced to the conclusion that the loans in question were loans made by the applicant-firm and that these loans were recorded in some other book or books of account which were not produced before the Income-tax Officer. He accordingly held that there was default in complying with the notice under section 22 (4) and made the assessment under section 23 (4).

The applicant-firm then presented an application under section 27 for the re-opening of the assessment. This application was rejected, as also the appeal to the Assistant Commissioner. A copy of the appellate order which reviews the evidence in the case is attached and marked " B. " * Thereupon an application under section 66 (2) for a reference to the High Court was made to the Commissioner and rejected by him. I wish to call attention to paragraph 8 of the Commissioner's order attached herewith and marked " C " * from which it is clear that the question of there being no evidence to support the finding of the Income-tax Officer and the Assistant Commissioner was not raised by the applicant before the Commissioner.

4. In my opinion both the Income-tax Officer and the Assistant Commissioner had before them ample evidence to support their conclusion that the applicant-firm had withheld a part of its accounts. This being so, the assessment had to be made under section 23 (4), and therefore the answer to the question formulated by the High Court should be in the affirmative.

Leach, for the Assesseees.

Gaunt, for the Crown.

JUDGMENT

The S. P. K. A. A. M. Chettyar firm of Rangoon was called on to make a return of its income for the year 1926-27 for the purposes of its assessment to income-tax for the year 1927-28. It returned its income at Rs. 28,818—6—6. On investigation the Income-tax Officer found that certain items of interest shown in the books of the M. M. firm of Wakema and the K. S. M. firm of Kayan as paid to the S. P. K. A. A. M. firm did not appear in that firm's accounts, and that there had been several transactions between those firms and the S. P. K. A. A. M. firm which did not appear in the latter firm's accounts. The only explanation given for the absence of these transactions from the books of the S. P. K. A. A. M. firm was that the transactions were dealings not of the firm but of certain of its partners personally. The Income-tax Officer was not satisfied with this explanation because the transactions appeared in the books of the other firms as dealings with the S. P. K. A. A. M. firm and because there was in those books and in the documents recording the transactions nothing to indicate or suggest that the transactions were

not dealings with that firm. He however gave the firm's agent time to get particulars from the partners with whom those dealings were alleged to have taken place and to produce the accounts relating to those transactions. The agent failed to give any further particulars or to produce any further accounts, and as he asserted that the firm had no accounts other than those which he had produced, the Income-tax Officer came to the conclusion that the accounts which were produced did not contain all the transactions of the firm and that a portion of the accounts was being withheld. He therefore proceeded to make what purported to be an assessment under section 23 (4) of the Act, and assessed the firm on a Rangoon income of Rs. 3,25,000.

No appeal lies against such an assessment but the assessee is entitled to apply under section 27 of the Act to have the assessment cancelled on the ground that he was prevented by sufficient cause from making a proper return, and the firm filed an application under that section which was dismissed. The firm then filed an appeal against the order dismissing its application but that appeal was dismissed. There is no question that these two orders were rightly made, because the sole question which arose on the application and the appeal was whether or not the firm was prevented by sufficient cause from making a proper return, and it is clear that the firm failed to prove that there was any sufficient cause for its default. The firm then applied to the Commissioner of Income-tax to refer to this Court certain questions of law under section 66 (2) of the Act. The Commissioner refused, but he was required by a Bench of this Court to state and refer the case under section 66 (3) of the Act. He has accordingly stated and referred the case.

The Income-tax Authorities' findings of fact are not open to review by this Court unless there is no evidence to support them, and in this case there is abundant evidence to support the Income-tax Officer's finding that the firm was in default. It follows that the Income-tax Officer was entitled to make the assessment to the best of his judgment under the provisions of section 23 (4) of the Act.

The only question which arises in the case is as to the power of this Court to hold that what purports to be an assessment to the best of the Income-tax Officer's judgment was not in fact such an assessment, and was therefore not a legal assessment.

It was said by a Bench of this Court in *P. K. N. P. R. Chettyar Firm v. The Commissioner of Income-tax, Burma* (1) that "when section 23 (4) says that the Income-tax Officer shall make the assessment to the best of his judgment, it means that he must make it according to the rules of reason and justice, not according to private opinion; according to law and not humour, and that the assessment is to be not arbitrary, vague and fanciful but legal and regular." It was also said that, since there is no appeal against an assessment under section 23 (4), the only remedy against an arbitrary assessment, that is against what is in effect a fine of unlimited amount, is the discretion of the Commissioner to review the assessment under section 33. With these remarks I agree, and it is clear that if the Commissioner is to be in a position to review such an assessment, the Income-tax Officer must state in his order the materials or reasons on which his judgment is founded.

In the present case the Income-tax Officer gave no reasons and no indication of the basis of his assessment of the firm's Rangoon income at Rs. 3,25,000. All that he said was that he determined the firm's income for the year at Rs. 3,25,000. So far as appears from his order that determination was entirely arbitrary and was based purely on private opinion. I realise, of course, that where an assessee withholds the materials for a regular assessment, the

assessment to the best of the Income-tax Officer's judgment must necessarily be to some extent arbitrary, but it must also be reasonable and the materials or reasons on which it is founded must be so stated that the Commissioner may be in a position to ascertain whether or not it is reasonable. In this case no reasons or materials have been stated and the effect of the order seems to be that the firm has been fined a very large amount.

I would hold that because the assessment in question was entirely arbitrary and did not purport to be founded on any materials or reasons beyond the Income-tax Officer's private opinion, it was an illegal assessment and I would direct the Commissioner of Income-tax to pay the S.P.K.A.A.M. firm's costs in these proceedings and in Civil Miscellaneous Application No. 135 of 1928 of this Court, advocate's fee in each case to be ten gold mohurs.

(331) IN THE HIGH COURT OF JUDICATURE AT MADRAS

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvven and
Mr. Justice Walsh*

[9th October, 1929]

P. L. S. K. R. Firm Assesseees.*
vs.

The Commissioner of Income-tax, Madras.

Indian Income-tax Act (XI of 1922) Sec. 4 (2)—Foreign profits, remittance of—Entry in foreign accounts—Source of remitted sums, proof of—Finding of the Income-tax Authorities—Question, if one of law for reference.

The assesseees carrying on money lending business in British India and at Ipoh were assessed under Sec. 4 (2) of the Income-tax Act on certain remittances into British India from their Ipoh business. At Ipoh three sets of accounts were maintained, one relating to the outstandings taken over from an older firm wound up, the second relating to the first agency of the assesseees and the third being the accounts of their second or current agency. The assesseees contended that the remitted sums shown in the first set of accounts were from out of capital being realisations of the old firm's outstandings and that the profits in the other two sets of accounts were not operated upon. The Income-tax Authorities held that from the accounts the moneys remitted could not be identified as sums derived from any specific source but must be taken to have been drawn from the funds at the assesseees' disposal at Ipoh.

On an application to the High Court under Sec. 66 (3) for a case to be stated,

Held, that on the finding that the assesseees had not proved by means of their accounts that the remittances were not profits liable to tax, the assessment was good in law.

Application under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Madras to state a case for the opinion of the High Court.

*Order of the Commissioner of Income-tax under Sec. 66 (2) of the
Indian Income-tax Act.*

The petitioners remitted Rs. 1,20,000 to British India in the year of account from their business at Ipoh. They claimed in the assessment proceedings that this

included profits to the extent of Rs. 10,800 only. The Income-tax Officer worked out the profit available for remittance which he found to be \$ 35,015, or Rs. 54,098 and in the absence of proof to the contrary concluded that the whole of this profit had been remitted. The petitioners did not then question the accuracy of the Income-tax Officer's figure.

At the appeal stage they repeated the contention that the profits remitted were only Rs. 10,800, but they claimed further that the profits available for remittance as worked out by the Income-tax Officer included two sums of \$ 4,321 and \$ 14,283 being sale proceeds of rubber and also that certain losses incurred abroad before April, 1922 should be taken into account, and that for these reasons the profit available for remittance ought to have been determined at \$ 6,618. The Assistant Commissioner examined the figures afresh, held that the receipts from the sale of rubber had been rightly taken into computation as moneys received in the course of the petitioners' business and that losses of 1921—22 and earlier years were not relevant to the question before him, and finally determined the amount of remittable profit at \$ 34,677 or Rs. 53,576 and confirmed the Income-tax Officer's decision subject to this slight alteration in the figures.

In the year of account the petitioners were maintaining three sets of accounts at Ipoh. One set related to the outstandings taken over from the old P. L. S. Firm, another to the first agency of the petitioners (P. L. S. K. R.) firm, and the remaining set to its second or current agency. The remittance of Rs. 1,20,000 was shown in the first of these sets of accounts and it was contended on this ground that it should be taken to have included only the profit shown in that set, and that the profits revealed by the other sets were not "operated upon". The Assistant Commissioner was quite right in refusing to accept this contention. On the evidence adduced, the moneys sent to British India cannot be identified as sums derived from any specific source but must be taken to have been drawn from the funds at the petitioners' disposal at Ipoh. Those funds consisted of capital and profit and it was rightly inferred, in the circumstances, that the whole of the profit had been withdrawn.

The petitioners have required me under section 66 (2) to refer to the High Court three alleged questions of law. These questions, and my comments thereon, are appended.

(1) "When an assessee carrying on business in a foreign place and receiving any remittance therefrom into British India in any year has proved through his accounts that the remittance was not received from the profits of the period prescribed in section 4 (2) of the Act but that it came from other sources at his command, will it be lawful to the Income-tax Officer to ignore this evidence altogether and to act on the presumption that when there is profit in a foreign business for the period mentioned above, so much of the remittance as did not exceed such profits should be regarded as having come from such profits regardless of the question to which source the remittance was actually appropriated." The question contains two important mis-statements of fact. The petitioners have not proved by means of the accounts that the remittance was not (to the extent indicated above) a remittance of profit liable to tax under section 4 (2). If they had done so that would have been an end of the matter. Nor is it true to say that the Income-tax Officer ignored the evidence of the accounts. He examined the evidence and decided that it did not amount to proof of the petitioners' case. His decision was that the remittance included profits of the relevant years amounting to a certain figure. It cannot be said that this finding of fact was perverse or that there were no materials for it. There is no question of law here, and the question stated does not arise out of the facts found in the case.

(2) "Whether income derived from rubber plantations possessed by an assessee in a foreign place can be regarded as income derived from business and

treated as such under section 4 (2) of the Act". It has been found as a fact that the sale of rubber forms part of the petitioners' business operations. The question is purely one of fact.

(3) "Whether such income can be considered as received in British India when as a matter of fact the produce derived from the plantation is sold in a foreign place and the sale proceeds realised in that place". It is true as a matter of general principle that income received as such in one place cannot again be received by the same person in another place. But section 4 (2) creates an exception to that principle by enacting that profit made and received abroad shall under certain conditions be regarded as income at the time of its subsequent receipt in British India. The profits referred to in the question have been found as stated above, to be profits of the petitioners' business carried on at Ipoh, and as such they fall within the purview of this provision. To hold that, as a matter of law, they could not have been received in British India would be to ignore the very existence of section 4 (2). If the finding had been that these profits were not profits and gains of a business, I agree that section 4 (2) would not have been applicable and that they would not have been taxable on receipt in British India if they had been previously received elsewhere. There is, I think, no dispute as to the way in which the law should be applied. What the petitioners are disputing is the finding of fact that the sale of rubber was part of their business in the year of account.

For the above reasons, I hold that no question of law arises and I decline to state a case for the opinion of the High Court.

The Advocate-General with K.S. Rajagopalachari, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT

In this application under section 66 sub-section 3, Income-tax Act, 1922, the Commissioner of Income-tax has been given notice to show cause why he should not refer certain questions of law for the determination of this Court.

The facts are in brief that the assessed firm had a branch or agency operating in Ipoh, Federated Malay States. There had been an older firm there, but this was wound up and the assets, in the shape of outstandings, divided between the partners. One half of these assets in this way fell to the share of the partners in the assessed firm and were shown as a credit in its general balance. During the income-tax year 1926-27 the Ipoh branch remitted four sums of Rs. 30,000, Rs. 1,20,000 in all, to British India. The contention which the firm raises is that these remittances were derived from realizations of the old firm's outstandings, and were therefore mainly capital. The Income-tax Department has declined to accept this explanation, and has acted upon the ordinary presumption that, to the extent that profits were made at Ipoh—about Rs. 53,000—the remittances were composed of these.

The learned Advocate General, who appears for the applicants, virtually has to argue that the Commissioner of Income-tax must accept as conclusive accounts and statements produced by the firm showing the source from which these remittances were derived; any less qualified proposition will not serve his purpose, because the matter becomes then one of evidence and the Commissioner's decision upon the evidence is final. It will be seen from the Commissioner's order dated 16th July 1927 declining to state a case for the determination of this Court that the claim was disposed of on the ground that the petitioners had not proved by means of their accounts, which the Income-tax Officer had duly examined, that the remittances (to the extent referred to) were not profits liable to tax. That being so, there is no question but

that the assessment is good in law. It is not our business to scrutinize the evidence but in view of certain aspects of it which have been brought to our notice during the arguments we may add that the collections of old outstandings, as made, appear to have been added to the general balance of the firm, and that the remittances were made from that general balance; further, that, upon the applicants' own showing (statement 4) when the first remittance was made on 31st July 1925, a sufficient sum had not yet been realized from the old outstandings to meet it. These circumstances suggest that the accounts themselves are not conclusive of, if indeed compatible with, the applicant's case.

We dismiss the application with costs. Advocate's fee Rs. 150.

(332) IN THE HIGH COURT OF JUDICATURE AT MADRAS

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice
Curgenven and Mr. Justice Walsh*

[11th October, 1929]

S. L. S. Chettiappa Chettiar	} Assessee.*
S. L. R. M. Ramaswami Chettiar	...	...	...
A. S. P. L. V. R. Ramaswamy Chettiar	...	...	...

vs.

The Commissioner of Income-tax, MadrasReferring Officer.

Indian Income-tax Act (XI of 1922), Sec. 4 (2)—Foreign remittances from Ipoh to Madras—Set off in Madras accounts against Ipoh's debts—Assessability as remittance of profits—Money-lending business—Loans on security of properties—Properties taken over and resold—Profits, if business profits.

The assessee, a Nattukottai Chetty carrying on money-lending business in partnership at Madras and Ipoh, had drawn on the funds of the Madras business for his personal expenses amounting to over Rs. 60,000 at the end of the account year. During the year of account, 1925—26, there were remittances from Ipoh to Madras exceeding 2½ lakhs which were more than sufficient to wipe off "debts" due from Ipoh to Madras against which they were set off in the Madras accounts. On the 26th March, 1926, the assessee wrote to the Ipoh agent asking him, after ascertaining the income of the year, to debit the assessee in the sum of Rs. 30,000 and credit Madras therewith and accordingly a credit entry was made in the Ipoh accounts but not in the Madras accounts during the account year. The Income-tax Officer assessed this sum under section 4 (2) of the Income-tax Act treating it as an appropriation by the assessee out of the remittances to the Madras business whose profits were negligibly small.

Held, that the remittances being credited and debited in the Madras firm's accounts in discharge of debts owed by the Ipoh business and no moneys having actually come into Madras in pursuance of the assessee's letter of the 26th March, there was no legal evidence to make the assessee liable as for any drawing of foreign profits.

In the course of the money-lending business the assessee's firm used to lend money to its debtors on the security of their properties and to take them over in full or partial discharge of the loans. The properties were retained awaiting a favourable resale, the

maintenance expenses charged to the business account and the receipts therefrom brought to the Adayam account. On resale, any surplus or deficiency was likewise taken over to Adayam account as a profit or loss of the business.

Held, that the profits realised from the sales were profits derived from business.

Hudson Bay Co. v. Stevens, 5 Tax Cases 424, Referred to.

Cases [O. P. Nos. 169, 170 & 171 of 1928] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, in compliance with the order of the High Court.

CASE

O. P. Nos. 170 and 171 of 1928.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Income-tax Act, XI of 1922.

2. The petitioner is a Nattukottai Chetti residing at Karaikudi in the Ramnad District within the jurisdiction of the Income-tax Officer, I Circle, Karaikudi.

3. He is the proprietor of a money-lending business and an aerated water factory in British India and a partner with a half share in a firm carrying on business in Madras in British India and in Ipoh and other places outside British India. S. L. R. M. Ramaswami Chettiar, son of his deceased brother, [S. L. S. Chettiappa Chettiar, his uncle] is the other partner in the firm.

4. In the course of its business at Ipoh the petitioner's firm generally advances money to its debtors on the security of their properties—mostly rubber gardens in the Federated Malay States. When it finds that its debtors are not financially strong or that they are not in a position to repay their debts the firm generally takes over the properties secured in full or partial discharge of the loans. Thereafter the firm maintains the property until a favourable opportunity offers for its re-sale. In the meantime the expenses that it incurs on the maintenance of the properties are charged to its business account and receipts from the yield of the properties are taken as the receipts of the business and brought to its Adhayam account. The capital employed in businesses like the one conducted by the petitioner's firm often includes a large proportion of borrowed capital and the interest paid on such borrowed capital is, as has been done in this case, charged as an expenditure of the business irrespective of whether the capital exists for the time being in the shape of lands and houses taken over or of loans pending with debtors. When the properties taken over are finally re-sold the difference between the price as it stands in the books and that realised therefrom is, if a surplus, taken over to the Adhayam account of the business as a profit and, if a deficiency, charged to the expenses account of the business as a loss. In this manner the profits that arose from the sale of such properties were included by the petitioner's firm in its Adhayam account.

5. In the course of the year of account, Krodhana, 13th April, 1925, to 12th April, 1926, there were remittances from the Ipoh to the Madras firm exceeding \$ 2½ lakhs. In the Madras ledger folio maintained at Ipoh these remittances were for the most part set off against "debts" due from Ipoh to Madras. The remittances from Ipoh to Madras were, however, more than sufficient to wipe out these "debts". Out of these amounts remitted to Madras a sum of \$ 60,000 was adjusted in this account as paid in two sums of \$ 30,000 each to the two partners—the petitioner and his nephew. The Madras accounts showed that the petitioner was drawing for his personal expenses on the funds of his Madras business to which he owed at the end of the year Rs. 60,619. The profits of his Madras business were negligibly small

and it was obvious that the petitioner would not have drawn on the capital of his Madras concern for his expenses at headquarters and thus depleted its resources. The Income-tax Officer was therefore of opinion that the petitioner was really drawing on the funds of the Ipoh business (in which he had large profits) and proposed to tax him to the extent of \$ 30,000 or Rs. 46,500, being that portion of the sums remitted by Ipoh to Madras which, according to the entries in the accounts at Ipoh, were intended for the use of the petitioner.

6. The petitioner objected to this on two grounds. The first was that the adjustment made in the accounts at Ipoh was made on the last day of the year and amounted to no more than a book adjustment. The Income-tax Officer held that there was no force in this contention as he was not treating the adjustment entry as evidence of a remittance on that date but only as evidence that the large remittances which undoubtedly took place during the year constituted to the extent of the \$ 30,000 a remittance to the petitioner, which in the circumstances stated in paragraph 5 above had to be treated as an appropriation of profits. The second objection was that in computing the profits of the Ipoh firm the Income-tax Officer erred in taking into account a sum of \$ 52,888 being the profits derived from the sale of properties and the produce grown thereon. It was contended that this sum represented an accretion to capital and not income from "business" within the meaning of the Income-tax Act. The Income-tax Officer held that the surplus from the sale of properties and the income from the produce grown thereon accrued or arose to the firm in the course of its business. He accordingly taxed the amount of \$ 30,000 (Rs. 46,500). A copy of the order of the Income-tax Officer is filed Exhibit A.*

7. The petitioner appealed against this order to the Assistant Commissioner but without success. An extract of the order of the Assistant Commissioner is filed as Exhibit B.*

8. The petitioner thereupon required me to state a case and refer for the decision of the High Court certain questions of law alleged to arise out of the order of the Assistant Commissioner. I declined to refer them. A copy of my order dated 7th August, 1927 is filed marked Exhibit C.*

9. The petitioner thereupon moved the High Court under section 66 (3) of the Income-tax Act and the High Court, by its order dated 14th December, 1928, has directed me to state a case on the following questions:—

1. "Whether there was any evidence before the Commissioner on which he could find that the dollars Thirty thousand (\$ 30,000) remitted from Ipoh to Madras during the year of assessment was remitted not in discharge of the debt owed by the Ipoh branch to the assessee but as the latter's share of the profits?"
2. "Whether the sum of dollars forty-eight thousand four hundred and sixty (\$ 48,460), dollars seven hundred and ninety-three (\$ 793), dollars one thousand two hundred and twenty-five (\$ 1,225), dollars one thousand eight-hundred and six (\$ 1,806), and dollars six hundred and four (\$ 604) amounting in all to dollars fifty-two thousand eight hundred and eighty-eight (\$ 52,888) can be held to be income derived from business and are not merely accretions of capital?"

10. *Question 1.*—The Income-tax Officer found that large remittances had been sent from the petitioner's Ipoh business to his Madras business during the year of account, that the petitioner was drawing large sums from his Madras business for

his expenses at headquarters, that the profits in the Madras business were negligibly small, that the petitioner had himself instructed his agent at Ipoh to adjust a sum of \$ 30,000 in his own account and \$ 30,000 in his nephew's if the profits of the business for the year permitted the adjustment and that an adjustment had accordingly been made in the Ipoh accounts the effect of which was to treat \$ 60,000 out of the large sums remitted to the Madras business during the year as having been appropriated by the petitioner himself and his nephew. On these facts the Income-tax Officer found that the appropriation amounted to an appropriation made from profits and the petitioner failed to prove that the sum of \$ 30,000 received by him was withdrawn from his capital. My opinion is that there was ample evidence before the Income-tax authorities to justify the finding.

I might add that an identical adjustment had been made in the Ipoh accounts in the year previous to the year now in question; the Income-tax Officer taxed the amount covered by that adjustment (to the extent to which profits were available at Ipoh) and the petitioner acquiesced in the assessment.

11. *Question 2.*—As I have observed in my order quoted above the petitioner's argument seems to be that the rubber gardens constituted capital in his hands and that any profit derived from their sale was an accretion to capital. What happened was that the former owners of those gardens were indebted to the petitioner's firm and the gardens were taken over in satisfaction of the debts. The gardens thus represented value received in the course of the business of the firm. That value was subsequently turned into money by the sale of the gardens and the produce grown thereon and I think it is quite clear that the profit or loss resulting from these transactions was a profit or loss of the petitioner's business. If the firm by the sale of the gardens and the produce grown thereon received anything over and above the sum originally advanced that was clearly (subject no doubt to certain expenses) a business profit. As observed in paragraph 4 above the petitioner's firm itself has treated these transactions in every respect as part and parcel of its money lending business. My opinion is that the income in question was derived from business.

CASE

O. P. No. 169 of 1928

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 65 (3) of the Indian Income-tax Act, XI of 1922.

2. The petitioner is a Nattukottai Chetty residing at Pudukkottai in the Ramnad District within the jurisdiction of the Income-tax Office, I circle, Karaikudi.

3. He is the proprietor of a banking business at Kammendine in Burma and is also a partner with a 7/8th share in another banking firm which carries on business at Kaulalampur in the Federated Malay States.

4. In the course of its business at Kaulalampur the petitioner's firm generally advances money to its debtors on the security of their properties, mostly rubber gardens, in the Federated Malay States. When it finds that its debtors are not financially strong or that they are not in a position to repay its debts the firm generally takes over the properties secured in full or partial discharge of the loans; and where the value of the security taken over is less than the debt due it writes off the difference as an irrecoverable loan. Thereafter the firm maintains the property until a favourable opportunity offers for its resale. In the meantime the expenses that it incurs on the maintenance of the properties are charged to its

business account and any receipts from the yield of the properties are taken as receipts of the business and brought to its "Adhayam" accounts. The capital employed in businesses like the one conducted by the petitioner's firm often includes a large proportion of borrowed capital, and the interest, paid on such borrowed capital is, as has been done in this case, charged as an expenditure of the business irrespective of whether the capital exists for the time being in the shape of properties taken over or of loans pending with debtors. When the properties taken over are finally resold the difference between the price as it stands in the books and that realised therefor is, if a surplus, taken over to the Adhayam account of the business as a profit and, if a deficiency, charged to the expenses account of the business as a loss. The profits and losses due to the resale of the properties are thus included in the results of the firm's banking business, and for purposes of assessment to income-tax the profits of the business are computed on the basis of these accounts.

5. During the year 1925—26 a sum of Rs. 1 lakh was remitted by the firm at Kaulalampur to the business at Kemmendine. The Income-tax Officer computed the profits of Kaulalampur business in that year to be \$ 50,528 and the petitioner's share to be \$ 45,755, or Rs. 70,747 and taxed this sum as profits of the Kaulalampur business received by the petitioner in British India. The petitioner contented before the Income-tax Officer that a sum of \$ 14,963 being the profits derived from the sale of properties as described in paragraph 4 above which the Income-tax Officer had included in his computation represented an accretion to capital and should not be treated as "income" of the business within the meaning of the Income-tax Act. The Income-tax Officer held that the surplus from the sale of properties accrued or arose to the firm in the course of its business and was not covered by the exemption contained in section 4 (3) (vii) of the Income-tax Act. An extract of the order of the Income-tax Officer relative to this point is filed as Annexure A.*

6. The petitioner appealed against this order to the Assistant Commissioner but without success. An extract of the order of the Assistant Commissioner is filed as Annexure B.*

7. The petitioner thereupon required me to state a case and refer for the decision of the High Court certain questions of law arising out of the order of the Assistant Commissioner and in my letter No. 491/27 dated 23—8—27 (O. P. No. 128 of 1928) I referred three questions. The question that I have now been directed to refer is one which I declined to refer on the ground that the issue whether or not the surplus received by the petitioner's firm represented profits derived by it in the course of its business was a question of fact and the findings of the Income-tax Authorities on this issue concluded the matter. An extract of my order is filed as annexure C.*

8. The petitioner thereupon moved the High Court under section 66 (3) of the Income-tax Act and in its order dated 29—10—28 the High Court has directed me to state a case and refer the following question: "Whether the sum of \$14,963 does not represent in law a casual accretion of capital."

9. As I have observed in my order quoted above the petitioner's argument seems to be that the rubber gardens constituted capital in his hands and that any profit derived from their sale was an accretion to capital. What happened was that the former owners of these gardens were indebted to the petitioner's firm and the gardens were taken over in satisfaction of the debt. The gardens thus represent value received in the course of the business of the firm. That value was subsequently turned into money by the sale of the gardens and I think it is quite clear that the profit or loss resulting from these transactions was a profit or loss of the petitioner's business. If the firm by the sale of the gardens

received anything over and above the sum originally advanced that was clearly (subject no doubt to certain expenses) a business profit. It cannot be called capital merely because it was at one stage represented by land and trees. It may be noted that the surplus or deficit has been treated by the firm itself in its accounts as a business profit or loss. My opinion is that the question should be answered in the negative.

10. The word "casual" is used in the question and this word apparently contains a suggestion that the sum now in dispute is covered by cl. (vii) of sub-section (3) of section 4. In regard to this my opinion is that the receipt of this sum was not of a casual return but was a receipt arising from business.

K. S. Krishnaswamy Ayyangar and R. Kesava Ayyangar, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT

O. P. Nos. 170 and 171 of 1928

KUMARASWAMI SASTRI, J.—The point referred to us for decision is whether there was any evidence before the Commissioner of Income-tax on which he could find that the \$30,000 remitted from Ipoh to Madras during the year of assessment was remitted not in discharge of the debt owed by the Ipoh branch to the assessee but as the latter's share of the profits and (2) whether the sum of \$48,460, \$793, \$1,225, \$1,806 and \$ 604 amounting in all to \$ 52,888 can be held to be income derived from business and are not merely accretions of capital?

The facts are shortly these. There was a firm in Madras and a firm in Ipoh carrying on money-lending business. The partners were the same. During the course of the dealings, moneys were due by the Ipoh firm to the Madras firm. The Ipoh firm was making profits in the accounting year 1925—26, the year of assessment being 1926—27. In the accounting year sums were remitted out of the Ipoh profits to the Madras firm, which in the Madras accounts were appropriated to wipe off the debt due to the Madras firm. The partner in the Madras firm who was also a partner of the Ipoh firm wrote a letter to the agent of the Ipoh firm on March 26th, 1926 the material portions of which run as follows: "As the debt due by us (Ipoh) to Madras has mostly been discharged it will not be convenient to send moneys to Madras and debit it. You may subject to the exigencies of the business there ascertain the income for the year ending Panguni 30th Krodhana (12—4—1926) and agreeably thereto debit the headquarters in the sum of \$30,000 on Sena's account and in \$30,000 on R.M's account and to credit Madras therewith".

According to this letter a credit entry was made in the Ipoh accounts but not in the Madras accounts in the year of accounting. The assessee has been taxed on this \$30,000 on the ground that it comes under section 4 cl. 2 of the Income-tax Act. Section 4 cl. 2 runs as follows:—"Profits and gains of business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that

year provided that they are so received or brought in within 3 years of the end of the year in which they accrued or arose". There is an explanation which is not necessary to consider for the purpose of this case. The effect of section 4 cl. 2 is that so far as the firm outside British India is concerned even though there may be a partner in British India he is not liable to pay income-tax on profits except in so far as any portion of the profits are brought into British India within the year of accounting.

What happened in this case was that moneys were sent from Ipoh to Madras and these were credited in the Madras firm's books. The net result was that the amount which Ipoh owed Madras was wiped out leaving a balance. There is no suggestion anywhere in the records that when these moneys were sent to the Madras firm they were credited in the Madras firm's books as profits received by each partner individually. *Prima facie* the Ipoh firm owed the Madras firm large sums of money and receipts were credited in the Madras partnership account. The assessee admits that the Madras firm will be taxable. In fact the assessee does not deny that this amount will be taxable as profits remitted to the firm and that it ought to be included in the next year's accounts. The Madras firm will be taxable irrespective of any drawings of the partners and that will be the ordinary state of affairs in the case of firms which are assessable under the Act.

Next as regards the applicant in the present case it is sought to make him liable for a portion of the money remitted to the Madras firm and the only ground on which he can be so taxed would be on the evidence of the letter referred to above. It is not suggested that any moneys actually came into Madras in pursuance of that letter during the year of taxation. The Income-tax Officer did not treat this letter as showing that any amount was received by the petitioner from Ipoh. It is used as evidence that the petitioner must have received the profits earned outside British India and they were debited in the firm's books. It is nobody's case that the entries in the firm's books were a mere blind for the purpose of enabling one partner to draw out the profits earned outside British India and thereby escape taxation. There is no question of any fraud suggested in any of the orders of the Income-tax Officers. What is said is that this letter evidences a receipt of \$ 30,000 by the assessee. We do not think that that letter shows anything of the sort. That letter was written asking the Ipoh agent to look into the accounts, ascertain the income for the year and debit the headquarters in the sum of \$ 30,000 on Sena's account and \$ 30,000 in R.M.'s account and to credit Madras therewith. This does not show that the entire profits for the year were ascertained and that the \$ 30,000 represented the profits remitted to the partner during the year of account. Where a partner draws moneys in the course of his business that will be taken into consideration at the end of the year and if there are any overdrawings by one partner they will be debited to the account of that partner or set off against his profits and because a partner draws some moneys during the year of account it cannot be said at once that that represents his share of the profits. Section 4(2) is for the purpose of ascertaining the profits of a partner got from business carried on outside British India and when such profits come into British India that will be taken into consideration in assessing him. • If a firm receives such profits from another firm it is the firm that should be taxed.

Further there is no evidence in this case that this letter showed either by itself or coupled with the other facts that any moneys remitted to the Madras firm during the course of that year were really remittances made to the assessee, and that it was sent to the Madras firm for the purpose of making the assessee escape liability to taxation. The reference is "Is there any evidence on which we can find that the \$ 30,000 remitted from Ipoh to Madras during the year of assessment was remitted not in discharge of the debt owed by the Ipoh branch to the assessee but as the latter's share of the profits". When the remittances were made they were all credited and

debited in the firm's accounts and were for the discharge of the debt owed by the Ipoh firm and under these circumstances we do not see any legal evidence to make the assessee liable for any drawing which he has made and which has been put down as in discharge of the debt owed by the Ipoh firm. In these circumstances we answer the first question in the negative.

Then as regards the 2nd question moneys realised by the sale of certain immovable properties, the finding of the Income-tax Officer is that these transactions took place as a matter of fact in the course of the business, that the properties were taken over with the intention of selling them and that the profit derived from the transactions as a whole including the sales was as much a profit of the firm's business as that derived from its other money lending transactions. The firm got these properties in discharge of debts due to it, resold the properties at a profit and the Income-tax Authorities consider this as a profit derived from its business.

It is argued by Mr. K. S. Krishnaswami Iyengar that the firm's business was only money lending and no profit realised by the sale of the properties got in satisfaction of the debts due to the firm can be said to be profit made in the course of the firm's business and so it is not liable to be taxed. Reference is made to *Hudson's Bay Co. v. Stevens* (1). We do not think that any general rule can be laid down in these cases. One has to see what is the course of dealing and though the business is labelled as money lending business, if as a matter of fact the profits were generally got by taking lands in satisfaction of debts due and selling them for profits later on, such profits must no doubt be considered as derived from such business and cannot escape taxation by saying that the profits have nothing to do with the business of the firm which was merely money lending. The finding of the Income-tax Authorities is that the profits represented the profits of the business and are not, as was contended, accretions of the capital. Further this case is analogous to that of a pawn-broker who lends out moneys on articles received as pledges which he sells in satisfaction of the amount due to him and realises profits. It cannot be said that the profits realised from such sales do not amount to profits derived in the course of the business.

In these circumstances we cannot say that the profits realised from the sale of the properties got by the firm in satisfaction of debts due to it were not got in the course of its business and that they were accretions of the capital. These were really profits which accrued in the course of the business and are thus taxable.

The petitioner is entitled to costs which we fix at Rs. 250 on each of the petitions. The advance paid by him of Rs. 100 will be refunded.

O. P. No. 169 of 1928.

Our order on point 2 in the above case holds good in this also and we dismiss it. The assessee will pay Rs. 250 as costs of the Commissioner.

(333) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri Kt., Mr. Justice Curgenvven and
Mr. Justice Pakenham Walsh.*

(14th October, 1929).

P. L. M. P. L. Palaniappa Chettiar

.. Assessee.*

vs.

The Commissioner of Income-tax, Madras

.. Referring Officer.

*Indian Income-tax Act (XI of 1922) Sec. 34—Income escaping assessment
—Proceedings to raise rate of tax—Income-tax Officer, if bound to re-assess
income or re-open items not in question.*

*An Income-tax Officer taking action under section 34 of the Income-tax
Act for raising the rate of tax on the ground that the rate originally fixed was too
low is only bound to confine himself to the particular item omitted and need not
reassess the income, that is, determine afresh the correct taxable income of the
assessee.*

Case (O. P. No. 168 of 1928) stated under Sec. 66 (3) of the Indian
Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, in com-
pliance with the order of the High Court.

CASE.

I have the honour to refer the following case for the decision of the
Hon'ble the Judges of the High Court under section 66 (3) of the Indian
Income-tax Act XI of 1922.

2. The petitioner is a Nattukottai Chetti residing at Puduvayal in the
Ramnad district within the jurisdiction of the Income-tax Officer, I circle, Karai-
kudi. He owns house property in his village where he also carries on a business
in money lending but the greater part of his income is derived from two firms in
Burma in each of which he is a partner.

3. For the assessment of the year, 1926-27, he made a return of income
in which he stated that he was a partner in the two firms mentioned above and
that he had no other income. When he appeared in response to a notice under
section 23(2) of the Act he admitted to the Income-tax Officer that he had income
from investments in Chetti firms in Burma and from moneys lent out at Pudu-
vayal and that he had no accounts or other evidence to prove the amount of such
income. The Income-tax Officer therefore acting to the best of his judgment
estimated the petitioner's income from money-lending at Rs. 10,000. The part-
nerships were being assessed separately in Burma and the petitioner's share of
income from them had to be taken into account under section 16 for purposes of
determining the rate at which tax had to be recovered on the income determined
by the Income-tax Officer. The Income-tax Officer had at that time no infor-
mation before him as to the amount of such income and as is usual in such cases,

he adopted an estimate in respect of that income "subject to communication from the Income-tax Officers concerned." The income from property was determined to be Rs. 125 and assessment was finally made as follows:—

	Rs.	Rs.
(a) Property	...	125
(b) <i>Business</i> :—		
(1) Local money lending	... 10,000	
(2) Income from partnerships (estimated).	18,000	
	—	28,000
Total income	...	28,125
Deduct income from partnerships (taxed elsewhere).		18,000
Taxable income	...	10,125

Tax at 1 anna in the rupee is Rs. 632-13-0. A copy of the order of the Income-tax Officer is filed marked **Exhibit A**.*

4. This assessment was made in June, 1926. The petitioner did not appeal against the assessment and the tax was paid on the 10th August, 1926. In September, 1926, the Income-tax Officer was informed by the Income-tax Officer, Henzada, (Burma), that the petitioner's income as a member of the partnership assessed there was Rs. 16,453. In January, 1927, he was similarly informed by the Income-tax Officer, Yamethin, that the petitioner's share of the income of the partnership assessed at Pyabwe was Rs. 15,808. Substituting these figures for the estimate of Rs. 18,000 adopted in the original assessment the Income-tax Officer found that the appropriate rate of tax was 18 pies (and not 1 anna in the rupee as was assumed in the original assessment). He accordingly issued a notice under section 34 of the Income-tax Act requiring the petitioner to show cause why tax should not be levied at 18 pies in the rupee on the taxable income of Rs. 10,125. A copy of this notice is filed marked **Exhibit B**.*

5. In reply to this notice the petitioner put in a return of income showing the following figures:—

	Rs.	Rs.
(a) Property	...	125
(b) (1) Share of income from the M.R.P.L.P. Firm, Henzada.	16,453	
Share of income from the E.K.S.P.L. Firm, Pyawbe.	15,808	
	—	32,261
(2) Business—Local investments	...	
Interest received	...	2,652
Interest due	...	158
Total.	...	35,196

6. Since the only question raised in the notice under section 34 was as to the amount of the income from the Burma partnerships (item (b) (1) above)

* Not printed.

and since the petitioner had accepted the Income-tax Officer's figures in respect of this item the Income-tax Officer purporting to act under section 23 (1) read with section 34 of the Income-tax Act at once made the assessment as proposed and levied additional tax. This was done on the 16th March, 1927.

7. The petitioner appealed to the Assistant Commissioner against the Income-tax Officer's decision under section 34 but the appeal was unsuccessful. A copy of the order of the Assistant Commissioner is appended marked Exhibit C.*

8. He thereupon put in a petition under section 66 (2), requiring me to state a case to the High Court which was dismissed by my order dated 26th July, 1927—a copy of which is filed marked Exhibit D.*

9. On a petition preferred to the High Court under section 66 (3) the High Court has directed me by its order dated 13th December, 1928, to state a case and refer the following question:—"When an Income-tax Officer takes action under section 34 of the Income-tax Act for the purpose of raising the rate of tax on the ground that the rate originally fixed was too low, is not the Income-tax Officer bound to re-assess the income, i.e., to determine afresh the correct taxable income of the assessee?"

10. In order to realise the precise scope of the question it is necessary to remember what the petitioner wants to secure. His income from sources other than partnerships, i.e., his taxable income had been fixed in June, 1926, and it included a sum of Rs. 10,000 at which his income from miscellaneous investments had been estimated, he himself having declared that he maintained no accounts in respect of this source of income. He did not appeal against that figure but acquiesced in the assessment and paid the tax. He apparently thought later that the figure was too high and considered that the issue of a notice under section 34 furnished a suitable opportunity to him to agitate for a revision of that figure. He accordingly came forward at that time with an offer to prove the amount of such income by the production of his headquarters accounts—accounts the existence of which he had totally denied at the time of the assessment but which he now said he had not produced in past "owing to sheer ignorance".

11. Section 34 of the Income-tax Act enacts:—"If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year or has been assessed at too low rate a rate, the Income-tax Officer mayproceed to assess or re-assess such income, profits or gains."

The object of section 34 is to enable an Income-tax Officer to impose further tax in either, or both of the following ways, viz., (1) to make a charge on income, profits and gains which being chargeable to income-tax have escaped charge, and (2) to make an additional charge on income which having already been charged to income-tax has been charged at too low a rate. The proceedings in this case were started for the purpose of the latter. The petitioner's income determined by the Income-tax Officer in June, 1926, consisted, as shown in paragraph 3 above, of (a) a sum of Rs. 10,125 on which tax was recoverable direct from the petitioner and (b) a sum of Rs. 18,000 on which tax was recovered elsewhere, (i.e., in the hands of the firms from which the income was received) and which came into account merely for purposes of determining the rate at which income-tax was to be deducted on the first sum. What the Income-tax Officer purported to do under the provisions of section 34 was: (a) to enhance the assessment of the petitioner's income from partnerships by raising it from Rs. 18,000 to Rs. 32,261, in order that he might be able (b) to re-assess

the taxable income of Rs. 10,125 at a higher rate, viz., at 18 pies per rupee, as against the rate of 12 pies per rupee originally adopted. He did not purport to do anything more. The petitioner does not object to the Income-tax Officer's action in enhancing the income from partnerships. Nor apparently does he dispute the Income-tax Officer's right to recover tax at the higher rate on the taxable income. What he does object to is to the Income-tax Officer's declining to determine afresh the amount of the taxable income (i.e., the income of Rs. 10,125) in such a manner as to reduce it to a lower figure. In my opinion section 34 does not authorise the Income-tax Officer to modify it in this manner.

12. I would therefore answer the question propounded above in the negative.

R. Kesava Ayyangar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question we are asked to answer is, when an Income-tax Officer takes action under section 34 of the Income-tax Act for the purpose of raising the rate of tax on the ground that the rate originally fixed was too low, is not the Income-tax Officer bound to re-assess the income, that is, to determine afresh the correct taxable income of the assessee? Section 34 refers to income escaping assessment and it provides that in such cases—it may either be that the income has escaped assessment, or has been assessed at too low a rate—the Income-tax Officer may serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included under sub-section (2) of section 22 and may proceed to assess or re-assess such income, profits or gains and that the provisions of this Act, shall, as far as possible, apply accordingly as if the notice were a notice issued under that sub-section. Then there is a proviso that the tax shall be charged at the rate at which it would have been charged had the income, profits or gains not escaped assessment or full assessment, as the case may be.

It is argued for the petitioner that under section 34, where the rate at which the tax is levied is sought to be raised, the Income-tax Officer is bound to begin proceedings again as regards assessment and in fact proceed as if there is an enquiry in respect of not only of the portion which has escaped assessment but of all the other items also; and reference is made to sections 14 and 16. It is argued that, when there are various heads under which a person returns his income, if in respect of one of those heads, owing to an omission or under-estimation he has been taxed at a certain rate which is subsequently found to be incorrect and notice is given to him under section 34, the Income-tax Officer is not to confine himself to that portion which has escaped assessment but he is to begin again as if the notice sent was a first notice sent to the assessee to return his income. We do not think that section 34 requires any such thing to be done. Section 34 refers to a specific case, namely, the case where an income chargeable to income-tax has escaped assessment or has been assessed at too low a rate. It may escape assessment leaving the rate unchanged, in which case it is only the amount of the assessment that will have to be raised owing to the rise in the taxable income, or it may escape assessment in such a way that, if rectified it would take the income beyond a certain rate, for example, it may give the figure to be over Rs. 40,000 in which case it will be assessed at 0-1-6 instead of 0-1-0 and the rate will therefore be higher. Where the rate is in question the enquiry need not, under section 34, go beyond

the facts on which the raising of the rate depends. When the assessee is given notice to show cause why the tax should not be raised because of an item having escaped assessment he is entitled to show that, as a matter of fact, there has been no omission and that the original rate is correct. We do not think that section 34 requires the whole thing to be re-opened and every item under which income-tax is charged to be considered afresh and a fresh assessment levied. In one sense, of course, he must fix the taxable income to enable him to fix the rate, but he is not bound to re-open the items which are not in question or which have become final and start proceedings again. We think he is only bound to confine himself to the particular item which has been omitted.

Our answer will therefore be that, in a case where the rate is sought to be raised under section 34 of the Income-tax Act, an Income-tax Officer is not bound to determine afresh the correct taxable income of the assessee. The petitioner will pay Rs. 250 the costs allowable.

(334) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvven and
Mr. Justice Pakenham Walsh.*

(15th October, 1929.)

O. R. M. O. M. S. P. Lakshmanan Chettiar

... Assessee.*

v.

The Commissioner of Income-tax, Madras

... Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 10—Money-lending business—Debtor's estate taken over in discharge of debt—Profits on re-sale, if assessable as business profits.

The assessee carrying on money-lending business took over in discharge of a debt due to him some simple money debts, mortgage debts and rubber plantations belonging to his debtor. The items taken over were entered in an account called Thundu Kanaku forming a separate ledger page in his business accounts, monies realised therefrom being credited in the general business accounts. In respect of the simple and mortgage debts, the assessee having recovered smaller sums than the amounts for which they were transferred was allowed to claim the deficiency as a business loss in his income-tax assessment for the year when he wrote it off in his accounts.

On an assessment of the profits from the sale of the rubber estate

HELD, that on the facts of the case the profits though derived from an isolated transaction were assessable as part of business profits.

Case [O. P. No. 179 of 1928] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras in compliance with an order of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Indian Income-tax Act, 1922.

2. The petitioner is a Nattukottai Chetti, residing at Devakottai in the Ramnad District within the jurisdiction of the Income-tax Officer, Karai-kudi (I) Circle.

* (1930) 58 M.L.J. 68 ; 31 L.W. 223 ; A.I.R. (1930) Mad. 121.

3. He is the proprietor of a banking business with branches situate in and outside British India one of which is at Madras.

4. In the course of his business at Madras he advanced various sums of money to one P. L. N. K. Subramaniam Chettiar. In or about October, 1922, the amount due by Subramaniam Chettiar amounted to about Rs. 53,000. At that time the petitioner pressed this debtor for the re-payment of the loan and as the latter was not in a position to discharge his liability in cash he assigned in favour of the petitioner cash outstandings, mortgages and rubber gardens at Penang of the face value of \$50,000 for a consideration of \$26,000 or Rs. 46,280. The petitioner gave credit to the debtor for this sum in his Madras accounts. The balance due from the debtor with interest thereon up to 1st Chithrai, Rakthakshi, (13th April, 1924), amounted to Rs. 11,733. About the end of December, 1924, the petitioner got an assignment of the debtor's interest in a decree in Penang for a consideration of Rs. 3,500 and a further sum of Rs. 2,500 in cash. After giving credit for the several sums received from the debtor a sum of Rs. 5,733 was still found to be outstanding and the petitioner wrote off this sum in his Madras accounts and claimed it as a deduction on account of bad debt in arriving at the profits of the Madras business taxable in the year, 1925-26. The Income-tax Officer allowed the petitioner's claim.

5. The outstandings, etc., which were assigned to the petitioner by P. L. N. K. Subrahmaniam Chettiar and referred to in paragraph 2 above were as under:—

	\$
Cash outstandings ..	32,450
Debt due from K. U. O. on mortgage of land	4,050
Rubber gardens	13,500
	<hr/> 50,000 <hr/>

In giving credit to the debtor for the sum of Rs. 46,280 or \$ 26,000, the consideration agreed upon, the petitioner debited K. U. O. in his Madras accounts with a sum of Rs. 7,087 or \$4,050 and debited the balance of \$21,950 to an account styled "Penang Thundu Account". Thereafter the petitioner instructed a money-lending firm at Penang in which he is a partner to realise the outstandings taken over from the debtor. A sum of Rs. 3,778 was collected from K. U. O. and during the year of account, the petitioner wrote off the balance due in the account, viz., Rs. 3,309 as irrecoverable and claimed it as a deduction in computing the profits of his Madras business. This claim was also allowed by the Income-tax Officer. The other assets valued in the books at \$21,950 actually fetched a profit of Rs. 70,000 on re-sale. Out of this a sum of Rs. 64,009 was received in Madras and credited to the "Penang Thundu Account". In the Profit and Loss statement filed by the petitioner before the Income-tax Officer in support of his return for the assessment of the year, 1926-27 (based on the profits of the period 13th April, 1925, to the 12th April, 1926) the petitioner showed this sum of Rs. 64,009 as the profit of his Madras business but claimed to deduct therefrom (1) Rs. 48,739 which he alleged represented the sale proceeds of rubber garden in the Malay States and (2) Rs. 7,247 taxed already in previous years as the profits of the Madras business. The Income-tax Officer allowed the second claim but as regards the income from the sale of rubber gardens he held that the petitioner took over the gardens in lieu of debts with the object of again converting them into cash at a favourable opportunity and that the profits which he had realised arose in the course of his business in money-lending and were part of the profits of that business. A copy of the order of the Income-tax Officer on this point is appended marked Exhibit A.*

7. The petitioner appealed against this order to the Assistant Commissioner, Southern Range, who agreed with the findings of the Income-tax Officer and dismissed the appeal. An extract from the order of the Assistant Commissioner relating to this point is appended marked Exhibit B.*

8. He then required me by an application under section 66 (2) of the Income-tax Act to state a case and refer for the decision of the High Court certain questions of law arising out of the order of the Assistant Commissioner which I declined to do for the reasons contained in my order dated the 17th January, 1928, a copy of which is appended marked Exhibit C.*

9. Thereupon the petitioner moved the High Court under section 66 (3) of the Income-tax Act and in its order dated the 12th March, 1929, the High Court has directed me to refer the following questions:—

(a) Whether the Assistant Commissioner is right in holding that the present case is outside the principle of the decision in *Secretary Board of Revenue v. Rm. Ar. Rm. Arunachalam Chettiar*(1) and

(b) Whether on the facts of this case the assessment of the sum of Rs. 48,739 is legal.

10. My opinion on question (a) as propounded above is that the Assistant Commissioner having found that the petitioner took over the gardens with the hope of realising a profit on re-sale was right in holding that the profit in question was liable to be taxed and that there is nothing against this view in the decision of the Madras High Court in *Secretary, Board of Revenue v. Rm. Ar. Ar. Rm. Arunachalam Chetty*.(1)

As regards question (b) the petitioner's argument seems to be that the rubber gardens constituted capital in his hands and that any profit derived from their sale was an accretion to capital. What happened in this case was that the former owner of these gardens was indebted to the petitioner and the gardens were taken over in part satisfaction of the debt. The gardens thus represented value received in the course of business. The value was subsequently turned into money by the sale of the gardens and I think it is quite clear that the profit or loss resulting from these transactions was a profit or loss of the petitioner's business. If the firm, by the sale of the gardens, received anything over and above that part of the sum originally advanced in satisfaction of which the gardens were taken over, the excess so received was clearly (subject no doubt to certain expenses) a business profit. It cannot be called capital merely because it was at one stage represented by land and trees. It may be noted that the surplus was treated by the petitioner himself in his Madras accounts as a business profit. I am therefore of opinion that the assessment of the sum of Rs. 48,739 was legal and that the question must be answered in the affirmative.

V. V. Srinivasa Ayyangar and R. Kesava Ayyangar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.†

In this case the facts are shortly these: The petitioner carried on business in money-lending in Madras. In the course of such business one P. L. N. K. Subramaniam Chetti owed him about Rs. 50,000. Subramaniam Chetti failed and to discharge his debt he transferred certain properties to the petitioner for 26,000 dollars. The items transferred consisted of monies due on simple money debts, monies due on mortgage items and also rubber plantations. As regards monies due on simple money debts the petitioner recovered a smaller sum than the amount for which they were transferred and he wrote off Rs. 5,733 in the

† Delivered by Kumaraswami Sastri, J.

accounts and claimed that this was a business loss and got a reduction of income-tax. As regards the mortgage items, while a certain portion of the mortgaged property was recovered, he was not able to recover the amount for which they were assigned and he also claimed it as a business loss and got a deduction. As regards the rubber estate it was sold at a profit and the question is whether that profit is taxable as part of the profits made by him in the business.

The contention of the petitioner is that this was an isolated transaction, that it cannot be said to form part of his business, that any profits on resale was not profit made in the course of business and that therefore it is not taxable. The Income-tax Commissioner's view was that having regard to all the facts of the case, it should be treated as a profit made in the course of business.

The questions referred to us are : "(a) whether the Assistant Commissioner is right in holding that the present case is outside the principle of the decision in *Secretary, Board of Revenue v. Rm. Ar. Rm. Arumachalam Chettiar*(1), and (b) whether on the facts of the case the assessment of the sum of Rs. 48,739 is legal." The decision in *Secretary, Board of Revenue v. Rm. Ar. Rm. Arumachalam Chettiar*(1), was that it is a question of fact in each case whether certain stray transactions of a merchant are really part of his business so that the profits arising therefrom can be taxed as profits arising from his business. It was held there on the facts that profits that accrued to a banker and money-lender from certain stray speculative purchases and sales of dollars in the Straits Settlements were taxable as profits arising from his business and were not exempt from taxation as arising from occupation of a casual nature within the meaning of section 3 (2) (viii) of the Income-tax Act of 1918.

The facts which we have set out show that these rubber plantations were got by the petitioner in order to liquidate a loan made by him in the course of his money-lending business. So far as the items which went to liquidate this debt are concerned, they consisted, as already stated, of some simple money debts, mortgage items and this item of property and they were all clubbed together in an account called "*Thundu kanakku*". This account was part of the business account and only formed a separate ledger heading there. In dealing with this transaction of the re-sale of the rubber plantations we must take into consideration what he did in respect of all the three items which were taken together to discharge the debt. It does not appear that there was any separate treatment as regards this item. They were all brought into *Thundu Kanakku*; as monies were realised they were credited to the general account as monies realised in the course of the liquidation of the debt; and they were brought in the business account. When there was a loss in two of the transactions the loss was claimed to be a deduction out of the business accounts. So that, as regards the other two items, it is clear that they were treated as loss arising from the business and as a business transaction. There was nothing, so far as we can see, in the accounts which distinguished this item from the other two items which were got by the petitioner. On the contrary we find that the expenses of the rubber estate were debited in the business accounts, the income therefrom was also credited in the business accounts and the profits, the excess of income over the expense, was shown as business profit made outside British India in the return.

So far as the contention that this was an isolated transaction is concerned, there is nothing in the authorities to show that the profits of such a single transaction cannot be treated as part of the business profits. On the contrary, there are cases where profits of a single transaction have been treated as part of the

business profits. We may refer to the case in *T. Benyon & Co., Ltd. v. Ogg*(1), where, the principles governing such cases have been enunciated. In that case, a company which was doing business as selling agents for Colliery Companies and also as commission agents for purchase of trucks, purchased certain trucks for themselves and made a profit out of it. The question arose whether this was a profit made in the course of the business. Sankey, J., deals with the question raised and he puts the matter clearly as follows: "In my view there is no question of law really in issue here. The law seems to me to be perfectly well settled, and the only question one has to determine is which side of the line this transaction falls on. Is it, as Mr. Latter contends, in the nature of capital profit on the sale of an investment? Or is it, as the Attorney-General contends, a profit made in the operation of the appellant company's business? Now that is very largely, as I think, a question of fact again." Then, the learned Judge refers to certain circumstances and gives reasons for holding that it is part of the business. The learned Judge observes: "I do not think it is possible to say that the mere fact that it was an isolated transaction at once takes it out of the category of chargeable property. I think in most cases an isolated transaction does not fall to be chargeable, but I think you have to consider the transaction and you cannot lay it down as a matter of law without regard to the circumstances that in this case the £2,500 is not chargeable."

This is also the effect of the decision in *Martin v. Lowry*(2), where also it was an isolated transaction, and this is also the principle laid down in *Commissioner of Income-tax, Bombay v. Purshottamdas Thakordas*(3), where a cotton merchant happened to liquidate the affairs of another cotton merchant who failed and made a large profit as commission and it was held that it was profit made in the course of business. The question is not in this case whether the petitioner intended to sell it at a profit but, whether, having regard to all the facts and the way in which he treated this property and the other two items which were got by him in discharge of the debt and having regard to all the attendant facts, it can be said that this was part of the business.

We cannot say in this case there was no evidence before the Commissioner of Income-tax, having regard to all the facts set out, for coming to the conclusion that this must be treated as part of the business profits and, as there was evidence to justify his conclusion, it is difficult for us to hold that he was wrong in making the assessment. We therefore answer the reference by stating that the Commissioner was right in assessing the petitioner in the manner he had done. The petitioner will pay Rs. 250 the costs of the Commissioner.

(335) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvin and
Mr. Justice Pakenham Walsh.

(15th October, 1929).

R. M. V. R. M. Virappa Chettiar

.. Assessee.*

v.

The Commissioner of Income-tax, Madras .. Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 10—Money-lending business—Purchase and sale of lands—Profits therefrom, when business profits—Practice of Nattukottai Chetties.

The assessee, a Nattukottai Chetty carrying on money-lending business in Singapore, purchased one item of property in 1919 and another in 1924 and sold

(1) 7 Tax Cas. 125.

(2) 11 Tax Cas. 297.

(3) 2 I.T.C. 8.

* (1930) 58 M.L.J. 95; 31. L.W. 173; A.I.R. (1930) Mad. 123.

them in 1926-27. *The Income-tax Officer proceeding merely on the general presumption of Nattukottai Chetties purchasing and selling lands as part of their money-lending business assessed the difference in prices as a business profit.*

HELD, that in the absence of evidence showing that the land income and expenses were brought into the business accounts, there was no legal evidence to justify the assessment.

Case [O. P. No. 262 of 1928], stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Madras in compliance with the order of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Indian Income-tax Act (XI—22).

2. The petitioner, a Nattukottai Chetti, is the managing member of a Hindu undivided family residing at Karaikudi in the Ramnad district within the jurisdiction of the Income-tax Officer, First Circle, Karaikudi.

3. The petitioner's family carries on banking business in various places of which Singapore is one.

4. During the year, 1926-27, the petitioner received remittances amounting to Rs. 54,023 from his Singapore business. These remittances included two sums of \$6,124 and \$14,195. The petitioner contended before the Income-tax Officer that these sums represented profits on sale of land, that they were of a capital nature and were not profits arising or accruing from any business and that they should not be taken into account in working out the taxable profits available for remittance. The Income-tax Officer rejected the petitioner's claim holding that the business of the petitioner in Singapore included the making of profits by the purchase and sale of properties and that the profits earned by these transactions were therefore profits from business and consequently taxable. An extract of the Income-tax Officer's order relevant to this point is filed marked as Exhibit A.*

5. The petitioner appealed to the Assistant Commissioner but without success. An extract of the Assistant Commissioner's order is filed marked as Exhibit B.*

6. The petitioner then required me to state a case and refer for the decision of the High Court the following question: "Whether when an assessee dealing in money-lending business purchases properties in auction and the said properties happen to be sold for a higher price later on, the difference could be treated as profits arising from business, or whether it is not merely the realisation of capital?" I declined to refer it. A copy of my order is filed marked Exhibit C.*

7. The petitioner thereupon moved the High Court under section 66 (3) of the Income-tax Act and the High Court has by its order dated 24th April, 1929, directed me to state a case on the following question: "Whether there is any evidence to justify the finding that the purchase and sale of lands formed part of any business which the assessee was carrying on".

8. It will be observed from the Income-tax Officer's order of assessment that the petitioner was not himself able to explain why he purchased the land. One explanation, if explanation it may be called, was suggested, viz., that the purchase was made "as a matter of acquisition of property." But it was not

explained for what purpose it was thought necessary to acquire property so far away from where the family resides and why again the property thus acquired should be sold later on. Another explanation was attempted before the Assistant Commissioner, viz., that the land was purchased in the belief that the petitioner's status and position in life would be enhanced if he owned a large extent of real or immoveable property. This explanation was rejected by the Assistant Commissioner and, in my opinion, rightly so, for not only had this explanation not been mentioned before the Income-tax Officer but the properties were neither so vast nor so valuable when they were purchased as to raise the status of the purchaser in any one's estimation. Besides the subsequent sale of the properties indicated clearly that this explanation could not possibly be the correct one. The petitioner thus failed satisfactorily to explain the object of the purchase. On the other hand there was the fact that the object of the business carried on at Singapore was to make fluid profits. It is well known that in the course of their business abroad and as a part of it Nattukottai Chettis purchase land and other properties when they are cheap, hold them until such time as they are able to sell them at a good price. During the period these properties are in their possession the income derived, if any, on the one hand and the expenses of maintenance, if any, on the other are included in their business accounts. Further, the capital employed in businesses like the petitioners often includes a large proportion of borrowed capital and the interest paid on such borrowed capital is charged as an expenditure of the business irrespective of whether the capital exists for the time being in the shape of property or loans to debtors. Thus for all practical purposes businessmen of the petitioner's type regard speculation in the purchase and sale of lands as a part of their profit-earning activities in the Malay States. The petitioner in this case had not proved that he purchased these properties for any purpose other than that of making profits by resale. The properties in question were purchased in auction at a time when the market was low and sold when (with a revival in the rubber trade) the market rose. The petitioner and his family reside in the Ramnad district and it was not shown how they were interested in immoveable property in the Federated Malay States except as a means of deriving profits by resale. In view of all these circumstances, I am of opinion that the Income-tax Officer had ample materials to justify his finding that the profits from the sale of land in this case were part of the profits of a business which the petitioner was carrying on at Singapore.

K. Rajah Ayyar and V. Ramaswami Ayyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question referred to us is, whether there is any evidence to justify the finding that the purchase and sale of lands formed part of any business which the assessee was carrying on.

The Income-tax Officer in this case proceeds on what he says is a well-known fact that in the course of their business abroad and as a part of it Nattukottai Chetties purchase land and other properties when they are cheap and hold them until such time as they are able to sell them at a good price and that during the period these properties are in their possession the income derived, if any, on the one hand and the expense of maintenance, if any, on the other, are included in their business accounts. In the present case there is no evidence afforded by the books that the income derived and the expenses incurred were included and made part of the firm's business accounts. All that appears is that these Chettis purchased one item of property in 1919 and another item of

property in 1924 and that these were sold in 1926-27. On this fact and on this general presumption which the Income-tax Officer thinks fit to draw in these cases he has treated the difference in prices as a business profit. There is no evidence about what was done with the income. The books are not before the Income-tax Officer and there is nothing to show that the income and expenses were, as a matter of fact, brought into the partnership accounts. There is nothing to show that the profits were made by the operation of the petitioner's money-lending business and were not in the nature of capital profits on the sale of an investment. As pointed out by Sankey, J., in *T. Reymond & Co., Ltd., v. Ogg* (1) ordinarily profit arising out of an isolated transaction outside the scope of the business does not fall to be chargeable as a business profit.

On these facts we are not prepared to say that there is legal evidence on which the assessee can be assessed on the ground that it is part of the profits of the business carried on. The petitioner will be entitled to his costs Rs. 250.

(336) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvin and
Mr. Justice Pakenham Walsh.*

(17th October, 1929).

Rm. Pl. S. Sivaswami Chettiar

Assessee.*

v.

The Commissioner of Income-tax, Madras . . Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 22 (4) & 23 (2)—Combined notice for appearance and production of accounts—Validity—Non-production of accounts—Assessment under Sec. 23 (4).

A combined notice under Secs. 23 (2) and 22 (4) of the Income-tax Act requiring the production of specified accounts and the personal appearance of the assessee is valid. Where after submission of return an assessee served with such a notice appears but fails to produce the accounts called for, an assessment can be made under Sec. 23 (4).

Case [O. P. No. 121 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, XI of 1922.

2. The petitioner—Rm. Pl. S. Sivaswami Chettiar—a banker, who is a resident of Pudukotta State carries on business in British India, his principal place of business being Coimbatore within the jurisdiction of the Income-tax Officer, Coimbatore Circle.

3. For the assessment of the year 1927-28 the Income-tax Officer, Coimbatore, sent him a notice under section 22 (2) of the Income-tax Act requiring

(1) 7 Tax Cas. 125.

* (1930) 57 M. L. J. 854 ; A. I. R. (1930) Mad. 127.

him to furnish a return of his income during the year ending the 31st March, 1927. A return signed by one "Rm. P. L. S. Tirupathi Mudaliar" showing a net income of Rs. 6,771-11-9 from business was filed before the Income-tax Officer. No evidence accompanied the return to show that Tirupathi Mudaliar had authority to submit the return on the petitioner's behalf. The Income-tax Officer accordingly returned the form to the petitioner directing him to resubmit it after affixing his signature to the verification in the return. The return was not re-submitted and the Income-tax Officer made the assessment under section 23 (4) of the Income-tax Act on the ground that the petitioner had failed to make a return. About three weeks later the petitioner filed again the return signed by Tirupathi Mudaliar and at the same time applied to the Income-tax Officer under section 27 for a re-opening of the assessment, but without success. He then appealed to the Assistant Commissioner and contended that the return submitted by his representative was a legal and valid return. The Assistant Commissioner set aside the assessment and directed the Income-tax Officer to make a fresh assessment on the basis of the return made by the representative.

4. On receipt of the Assistant Commissioner's order the Income-tax Officer called on the petitioner under section 23 (2) of the Income-tax Act to adduce evidence in support of his return. One Rm. Pl. S. Sitarama Ayyar (whom the petitioner acknowledged at a subsequent enquiry as his authorized representative) applied for a week's time as he had written to his principal in the Pudukkotta State for some of the accounts of the business which were then with him. This was granted. On the adjourned date one Rm. Pl. S. Chockalingam Chettiar (whom also the petitioner acknowledged at the enquiry referred to above as his authorized representative) produced some of the accounts and put in a "revised written statement" showing a net income of Rs. 25,272. The Income-tax Officer found that certain old accounts relating to one of the businesses carried on by the petitioner, viz., the business at Sulus had not been produced. He accordingly directed the representative to produce those accounts and adjourned the case to the 29th November, 1927. Mr. Sitarama Ayyar referred to above appeared on that date with the 'old accounts' called for and submitted another "revised written statement" asking that a certain amount of loss said to have been incurred in the old accounts of the Sulus business should be deducted from the amount shown in the first "revised written statement" submitted by the other representative Chockalingam Chettiar. The Income-tax Officer examined the accounts and found that the old account disclosed a profit of Rs. 11,709.

5. In the course of the further enquiries made by him the Income-tax Officer had reason to believe that the petitioner maintained a set of accounts in which a portion of the profits derived by him was shown and the production of which he had been evading. He therefore issued to the petitioner a notice in form No. 86 (a combined notice under sections 22 (4) and 23 (2) of the Income-tax Act) directing him to appear before him and produce certain specified accounts, viz., the accounts in which certain money-lending and other transactions detailed by the Income-tax Officer in the notice were recorded. An attempt was made to serve this notice on the petitioner in person but as the petitioner could not be found the notice was affixed to the door of the business premises. From his previous experience of the petitioner's attitude however the Income-tax Officer was of opinion that it was desirable to effect a clearer service of the notice and he accordingly sent another notice in the same terms by registered post. This was acknowledged by Mr. Sitarama Ayyar referred to above. In response to this notice the petitioner appeared through his Vakil but did not produce the particular accounts in which the transactions referred to by the Income-tax Officer were recorded. When questioned about them the

Vakil stated that he could not explain anything as Sitarama Ayyar, the petitioner's agent, (the agent who had acknowledged the notice) was away. The Income-tax Officer did not believe the statement about the agent's absence. And in any case it was clear that the petitioner had failed to comply with the terms of the notice issued to him under sections 23 (2) and 22 (4). The Income-tax Officer accordingly assessed him under section 23 (4).

6. The petitioner applied to the Income-tax Officer under section 27 of the Income-tax Act to re-open the assessment and contended that he did not maintain any accounts recording the transactions referred to by the Income-tax Officer in his notice under section 22 (4), and that there was therefore no failure on his part to comply with the terms of that notice. The Income-tax Officer refused to believe in the petitioner's statement and dismissed the application. A copy of his order is enclosed marked Exhibit A.* (Though it is not perhaps strictly relevant it may be mentioned here that the petitioner produced in the course of the assessment for the subsequent year, viz., the year 1928-29, the very accounts the existence of which he had denied in his application to the Income-tax Officer referred to above).

7. Against the order of the Income-tax Officer under section 27 the petitioner appealed to the Assistant Commissioner but without success. A copy of the Assistant Commissioner's order is filed marked Exhibit B*.

8. The petitioner now requires me to state a case and refer for the decision of the High Court the following questions:—

(I) Whether a combined notice under sections 23 (2) and 22 (4) is a valid notice, and whether on a non-compliance of the terms of such a notice an assessment under section 23 (4) could be justified? and

(II) Whether in respect of an assessee who has submitted a return of his income under section 22 (2), a notice issued under section 22 (4) is valid so as to justify an assessment under section 23 (4) in the event of non-compliance of the terms of the notice?

9. My opinion thereon is as follows:—

Question (I). The petitioner's argument is that the notice is invalid because it called on him to appear before the Income-tax Officer on a certain date and to produce certain accounts specified therein, while a notice under section 23 (2) could only direct him to appear before the Income-tax Officer or to produce the evidence which he had in support of the return. The answer to this argument, as the Assistant Commissioner has pointed out in his order, is that there is nothing in the Act preventing an Income-tax Officer from requiring an assessee under section 23 (2) to be present before him and at the same time requiring him under section 22 (4) to produce any specified accounts or documents.

As regards a combination of the two requirements in one notice the validity of such a notice was the subject matter of a decision by a full bench of the Calcutta High Court in the case of *Harmukhari Dulichand*(1), and Rankin, C. J., in the course of his judgment observed: "The first question is whether there is anything illegal in the issue of notice under sections 23 (2) and 22 (4). I am of opinion that there is no reason why these two notices should not be combined in one document. The position is that the assessee is given one date on which he is first of all to produce certain accounts or documents required by the Income-tax Officer and he is also told that on the same

date he will get an opportunity of producing any further evidence upon which he relies. I can see no objection at all to this procedure and I observe that in the case cited to us from the Allahabad High Court decided on the 4th January of this year (*Chandra Sen Jaini*) a Division Bench of that Court was of the same opinion. In my judgment there is no difficulty upon the answer to the first question'. I would respectfully adopt this reasoning and answer the question propounded in the affirmative.

Question (II). A similar question was answered in the affirmative in the case of *Rm. S. Rm. Ramaswami Chettiar vs. Commissioner of Income-tax, Madras*(5), by a Full Bench of the Madras High Court consisting of the Chief Justice, Mr. Justice Beasley and Mr. Justice Reilly.

For the reasons contained in their Lordships' judgment I would answer this question also in the affirmative.

K. V. Krishnaswami Aiyer and V. Rajagopala Aiyer, for the Assessee.
M. Patanjali Sastri, for the Crown.

JUDGMENT

KUMARASWAMI SASTRI, J.—The points referred to us for decision are (1) whether a combined notice under sections 23 (2) and 22 (4) is a valid notice, and whether on a non-compliance of the terms of such a notice an assessment under section 23 (4) could be justified? and (2) whether in respect of an assessee who has submitted a return of his income under section 22 (2), a notice issued under section 22 (4) is valid so as to justify an assessment under section 23 (4) in the event of non-compliance of the terms of the notice?

As regards the first point we think it is covered by authority. That a combined notice may be sent has been held in *Harmukhrai Dulichand v. Commissioner of Income-tax, Bengal*(1), *Chandra Sen Jaini v. The Commissioner of Income-tax, U. P.*(2), *R. M. P. Chettyar firm, v. Commissioner of Income-tax, Burma*(3), *Ram Kissendas Bagri v. The Commissioner of Income-tax, Bengal*(4).

The second question has, we think, been practically answered in *Ramaswami Chettiar v. Commissioner of Income-tax, Madras* (5). If a combined notice can be issued, there is nothing to prevent the Income-tax Officer from sending a notice, as he has done, in Form B, requiring the production of accounts which he wants to be produced and are specified on the back of his notice and also requiring the person to appear personally. Now, in cases where a person appears but does not produce the accounts he is asked to produce, we think the penalty under section 23 (4) can be applied. It is not necessary that another notice should be sent under section 23 (2) because under section 23 (4) any one of the defaults is sufficient to attract the provision that the Income-tax Officer can assess on the best of his information. The argument of Mr. Krishnaswami Ayyar, as we take it is, where a return has been submitted and even in cases where the Income-tax Officer acts under section 22 (4) and wants the production of accounts, he must still issue a notice under section 23 (2) and act after issuing that notice. That is reading into section 23 (4) what is not there. An Income-tax Officer is not bound to make up his mind the moment he receives a return as to whether he accepts it or not; it is open to him before he deals with the question to call for the production of accounts

(1) 3 I. T. C. 198.

(2) 3 I. T. C. 17.

(3) 3 I. T. C. 385.

(4) 2 I. T. C. 324.

(5) 3 I. T. C. 290.

and, as the accounts have to be proved by somebody, to call the assessee to appear in person. If the assessee appears in person but does not produce the accounts there is no reason to say that the penalty under section 23 (4) is not attracted simply because another notice has not been sent under section 23 (2) asking him to attend office and produce or cause to be produced any records which he may rely on in support of his return. This would presuppose that the Income-tax Officer must work his mind at once one way or the other and then act and that he cannot suspend judgment until he calls for the person assessed to substantiate his return, or calls for the accounts to substantiate his evidence.

We think both these questions have to be answered against the petitioner; that a combined notice is valid and that an assessee can be assessed under section 23 (4) in the event of non-compliance with the terms of the notice requiring the production of accounts which the officer in law is entitled to call upon him to produce. The petitioner will pay the costs of the reference, Rs. 250.

(337) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Cargenven and
Mr. Justice Pakenham Walsh.*

(18th October, 1929).

A. Suppan Chettiar & Co.

Assessee.*

vs.

The Commissioner of Income-tax, Madras ... Referring Officer.

Indian Income-tax Act (XI of 1922) Sec. 10 (2) (vi)—Depreciation allowance—Unabsorbed allowance of a business—Right to set off against profits from other businesses or other sources.

Where the profits and gains of a business are insufficient to cover the full depreciation allowance under section 10 (2) (vi) of the Income-tax Act on the machinery, plant, etc., used for the purposes of that business, the excess depreciation can be set off against the profits and gains of other businesses or from other sources.

Case [O. P. Nos. 16 and 244 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922) by the Commissioner of Income-tax Madras, for the opinion of the High Court.

CASE

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (2) of the Indian Income-tax Act, XI of 1922.

2. The unregistered firm of A. Suppan Chetti & Co. hereinafter called the firm are assessee on the file of the Income-tax Officer, Dindigul. They carry on the following businesses: (1) Grocery and Rice, (2) Money lending, (3) Soda factory, (4) Rice Mill, (5) Foreign liquor shops, (6) Motor service. For the assessment of the year 1927-28 based on the profits of the calendar year 1926 the firm returned an income of Rs. 2,745 from property, Rs. 253 from their motor business and Rs. 65,189 from their other businesses and claimed an allowance of Rs. 10,542 on account of depreciation in their motor business against

* (1930) 58 M. I. J. 46; A. I. R. 1930 Mad. 124.

the profits of that business to the extent to which they were available (viz., Rs. 253) and the balance against the profits of their other businesses. The Income-tax Officer allowed only the sum of Rs. 253 and disallowed the balance, holding that as there were no profits and gains in the motor business against which the balance of the depreciation could be allowed it should be added to the amount of the depreciation due for the following year under proviso (b) to section 10 (2) (vi). After disallowing other inadmissible expenses the Income-tax Officer determined their total income at Rs. 97,822 and levied income-tax and super-tax on this basis.

3. Against the disallowance of their claim on account of depreciation the firm appealed to the Assistant Commissioner but without success. A copy of the Assistant Commissioner's order is appended as Exhibit A*.

4. The firm now require me to state a case and refer for the decision of the High Court the question of law arising in the case. I refer the following question:—"Whether where an assessee owns a number of businesses A, B, C and D and the profits and gains of business A are insufficient to cover the full depreciation admissible (under section 10 (2) (vi) of the Act) on the machinery plant, etc., used for the purposes of that business, the excess depreciation can be set off against the profits and gains of other businesses B, C and D?"

5. The firm's contention in their written application to me for the reference was that the allowance of the claim for depreciation had the effect of reducing the profits and gains of the motor business to a loss of Rs. 10,289 and that they should have been permitted to set off this loss against their income from the other businesses that they carried on. During the argument of the case before me however they adopted a different ground and claimed that the various activities of the firm constituted one business and that the depreciation due in respect of the motor service (which according to them was only one department of their business) should be set off against the profits and gains of all their activities put together. I accordingly sent back the case to the Income-tax Officer and directed him to examine the conditions and circumstances under which the firm's affairs are carried on and report on the question whether the various concerns of Suppan Chetty & Co. are departments of the business as contended by the firm or are distinct businesses. The following facts are reported by the Income-tax Officer:—

"The assessee's business activities cover the following branches:— (1) Grocery and Rice, (2) Money Lending, (3) Soda Factory, (4) Rice Mill, (5) Foreign liquor shops and (6) Pankajam Motor Service. I first deal with the procedure followed by the assessee in regarding their business transactions from various concerns and then refer to the question of establishment, business premises, etc. The place of business for items Nos. 1 to 5 is Bodinayakanur and there are no branches in respect of these business activities outside Bodinayakanur, barring two foreign liquor shops on the Travancore hills. (The income from these shops is also incorporated in the head office accounts at Bodinayakanur). As regards Motor service, there are 4 branch offices, viz., at Periyakulam, Kodaikanal Road, Kodaikanal Hills and Uthamapalayam, the head office being at Bodinayakanur. The daily business transactions relating to all sources are passed through a parent day book kept at Bodinayakanur, e.g., details of collections and expenditure for every bus received daily from the various branch agents are posted in the day-book then and there, as found in the remittance

memorandum sent by the branch agent (I deal in a separate paragraph with the conditions and circumstances under which the motor service is conducted). Similarly, all business transactions connected with grocery, rice, money lending, are first passed through the parent daybook. From the daybook, postings are made into different ledgers, e.g. items relating to grocery and rice, and liquor shops are posted into a ledger called the "A" ledger. Transactions connected with the soda factory and rice mill are carried to the "E" ledger. Transactions relating to money lending are posted into the "C" ledger. A separate ledger called the "M" ledger is maintained for noting collections and expenditure for motor service. The receipts and expenditure are picked out from the parent day-book and are merely debited or credited as the case may be into the "M" ledger. This ledger is subsequently journalised for convenience of posting into separate personal and impersonal accounts.

Motor service. As mentioned above, there are four branches with headquarters at Bodinayakanur. In these branches, no other business except that of motor business is being carried on. The employees in these branch offices attend to no work other than the motor business. The system followed in recording the transactions is as follows: From the various branches daily remittance memoranda accompanying advices of collection for each bus and the expenditure incurred on that date are received by the head office. These daily remittances are passed through the parent daybook. In addition to the daily memoranda of collections and expenditure, there is a monthly chittai prepared by the branch agents by the help of the duplicates which they keep with them and the daybook is verified at the end of the month, with the help of this chittai. No other accounts except these duplicates of the daily remittance and expenditure memoranda are maintained at the branch offices. I have already stated that from the parent day book, the receipts and collections are picked out and entered in the "M" ledger. These receipts and collections are subsequently journalised, according to the nature of the transactions and postings effected in the various personal and impersonal accounts. Considering the question from the view point of accounts, it cannot be said that separate and distinct accounts are being maintained for separate businesses.

Salary to establishment, etc.... The "A" ledger which is the most important ledger and in which all final adjustments and results are incorporated contains the names of the employees who attend to the actual maintenance of accounts and supervision of the business as a whole, e.g., the name of Mr. Chammana Ayyar alias Venkateswara Ayyar, the Head Clerk, who supervises the business as a whole is to be found in this ledger. The ledger folio for the salary account contains debits and credits in respect of four persons. The monthly debits in respect of these persons aggregate to about Rs. 460. The salary, etc., paid to the staff working in the soda factory and rice mill is to be found in the "E" ledger which contains the personal accounts for these employees. The book of original entry for these ledgers is of course the parent day-book. The personal accounts for all employees connected with the motor service is to be found in the ledger kept separately for that part of the business. Advances to fitters and drivers, repairs, oil and petrol charges, salary and allowances paid to employees and expenditure connected with the motor work-shop at Bodinayakanur, are all found in this ledger. So far as the technical staff is concerned, it could be said that there is a separate establishment for motor service, but the service of the Head Clerk as also those of the second and third clerks are utilised partly in posting the ledger and writing up of the parent day-book.

which is the book of original entry. The Head Clerk also supervises the general working of the service

Premises.—No separate business premises are maintained for separate businesses. Barring the four branch offices for the motor service, viz., at Periyakulam, Kodaikanal Road, Kodaikanal Hills and Uthamapalayam, there is only one office at Bodinayakanur where all businesses are carried on.

The motor service is being conducted from the year 1914 onwards. The workshop was at first situated at Kodaikanal Road for some years. The assesseees tell me that a journal and a ledger relating to the transactions of the motor service were being maintained at those places, till the date on which the workshop was transferred from Kodaikanal Road to Bodinayakanur. Even at that time, the assesseees tell me, the receipts and collections were being passed through the day-book at Bodinayakanur just as it is now being done”.

7. The firm's case is that the various activities in which it is engaged constitute one business. These activities have been treated by the Income-tax authorities below as distinct businesses and the question to be decided is whether the facts set out above justify that conclusion. This question is one of fact. Mr. Justice Rowlatt in the case of *Scales v. George Thompson & Co., Ltd.*(1), in discussing the question whether the businesses carried on by a Company are to be regarded as distinct businesses or one business has remarked that the real question for decision in such cases is whether there is any inter-connection, any inter-lacing, any inter-dependence, any unity at all embracing the businesses in question and that if there is none they are distinct businesses. Looked at from this stand-point it seems to be that in the present case the various businesses carried on by the firm have no kind of connection. The firm could discontinue any one of its activities without detriment to the rest. There is no unity embracing all these activities except the fact that they are the activities of a single firm. It would be difficult to imagine a case in which it could be said with greater certainty that one person was carrying on several businesses. I therefore find as a fact that the business known as the Pankajam Motor service is one of several distinct and separate businesses carried on by the petitioner firm.

8. My opinion on the question of law set out in paragraph 6 above is as follows: Section 10 of the Indian Income-tax Act, XI of 22 enacts that “tax shall be payable by an assessee under the head “business” in respect of the profits and gains of *any* business carried on by him”, and under sub-section (2) to that section “*such profits* and gains shall be computed after making the allowances” provided therein. One of such allowances is in respect of insurance against risk of damage or destruction of buildings, machinery, plant, etc., used for the purposes of the business—Section 10 (2) (iv). “The business” referred to means “any particular business of which the profits and gains are being computed”. Lower down comes another allowance, viz., “in respect of depreciation of such buildings, machinery, plant or furniture being the property of the assessee.” Section 10 (2) (vi) and proviso (b) to that clause enacts that “where full effect cannot be given to any such allowance in any year owing to their being no profits or gains chargeable for that year or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given as the case may be, shall be added to the amount of the allowance for the following year.....” “Such buildings, machinery, etc.” in the above clause clearly means “buildings, machi-

nery, etc., used for the purposes of the particular business of which the profits and gains are being computed; and "no profits and gains" in the proviso similarly means "no profits or gains of the particular business of which the financial results are being computed."

Reading these various provisions it seems to me that tax is payable in respect of the profits or gains of each separate business and that under sub-clause 2 of that section such profits and gains, i.e., the profits and gains of each separate business, have to be computed separately. In computing the profits of each business the allowance for depreciation provided for by section 10 (2) (vi) should be allowed to the extent to which there are profits available in that business and the balance should be carried forward to the next year—Proviso (b) to section 10 (2) (vi). As the motor business carried on by the firm, which I have found to be a distinct business, made only a profit of Rs. 253 the firm was entitled under proviso (b) to section 10 (2) (vi) to carry forward to the next year the depreciation claimed by them in respect of that business in excess of this profit; but they are not entitled to have the excess set off against the profits of their other businesses. The special provision in the Act to the effect that such excess depreciation should be carried forward to the next year shows that the excess is not a loss of profits or gains to which the principle of section 24 applies.

T. M. Krishnaswami Aiyer and T. P. Gopalakrishna Aiyer, for the
Assessees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question which the Commissioner refers to us is "Whether where an assessee owns a number of businesses, A, B, C and D and the profits and gains of business A are insufficient to cover the full depreciation admissible under section 10 (2) (vi) of the Act on the machinery, plant, etc., used for the purpose of that business, the excess depreciation can be set off against the profits and gains of the other businesses B, C and D?"

The assessee is an unregistered firm carrying on the businesses of (1) grocery and rice, (2) money lending, (3) soda factory, (4) rice mill, (5) foreign liquor shops, and (6) motor service. The profits of the last-named, the motor service for the year to which the assessment relates, amounted only to Rs. 253, whereas the firm claimed an allowance of Rs. 10,542 on account of depreciation. Under section 10 (2) (vi) of the Act in computing the profits or gains of a business allowance may be made, within certain prescribed limits, in respect of depreciation of buildings, machinery, etc., and the question we have to answer is whether, taking this case as an example of the general proposition addressed to us, the allowance may be set against not only the small profit of Rs. 253 earned by the motor-service but against the profits earned by the other five businesses.

Section 10, which deals with the assessment of a business to tax, provides that the profits or gains shall be computed after making allowances in respect of charges classified into nine divisions, examples of which are rent, cost of repairs, interest on borrowed capital, etc. Admittedly in respect of each of these charges except depreciation it is open to the assessee to include the whole sum which it represents in his balance sheet, with the result, it may be that a

minus balance or loss on the business is shown. Then, if he has more than one business, or even more than one head of income as described in section 6, he is entitled under section 24 to set off the loss in the business against any profits or gains received under another head. In other words, if the charge is any one of those named in section 10 other than depreciation, the question which the Commissioner refers to us must, upon the plain terms of the Act, be answered in the affirmative.

It is said however that allowance for depreciation stands upon a different footing from the other allowances, and, as an indication of this, our attention is directed to proviso (b) under clause (vi) of section 10 (2). It lays down that "Where full effect cannot be given to any such allowance in any year owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or if there is no such allowance for that year, be deemed to be the allowance for that year, and so on for succeeding years." Taking the words "Profits or gains chargeable for that year" to refer only to the profits or gains of the business in which the depreciation occurs, it is contended that this proviso allows only one way of treating the charge; that so much of it as cannot be neutralised by profits must not figure as an actual loss, but must be carried forward into the next year's account. But neither from the language used, nor from any general considerations arising from the nature of the charge are we satisfied that this construction is correct. But for the proviso, depreciation stands upon the same footing, and should, so far as any intention to the contrary appears, be dealt with in the same way, as the other charges enumerated in the section; and it is a well-known principle of construction (see *West Derby Union v. Metropolitan Life Assurance Society*(1)), that a proviso should not by mere implication withdraw any part of what the main provision has given. We do not think therefore that upon the terms of the section an assessee is precluded from adding the whole charge for depreciation to his other business charges, even though the result is to show a loss, and then claiming under section 24 to set off the loss against profit from other sources. Nor have we been shown that there is anything in the nature of this allowance for depreciation to render such a course inadmissible.

The learned advocate for the Crown argues that it is not a business expense or loss, but rather a sum set apart to make good a loss of capital. There is an observation in *In re. The Spanish Prospecting Co., Ltd.*(2) that depreciation is a business loss. That however was not an income-tax case, and no doubt there may be a business loss of capital as well as of profits. We do not propose to pursue this line of inquiry further, as we have heard nothing in any sense conclusive upon that point. But it may be observed that a close analogy exists between money spent upon repairs to buildings, machinery, etc., and money set apart in respect of depreciation of such things, and that so far as we can discover there is no reason to treat differently the allowances in respect of these two classes of expenditure.

We have dealt with the question on the footing that the words "business" and "any business" occurring in section 10 (1) relate only to the business in which the depreciation occurred—in this case the motor service. If however

(1) (1897) A. C. 647.

(2) (1911) 1 Ch. 92.

we construe "any business" as meaning all the businesses put together, which was the construction put upon it in *Commissioner of Income-tax, Madras v. M. Ar. Ar. Arunachalam Chettiar*(1), then in proviso (b) "profits or gains" will mean the aggregate profits or gains of all the businesses together, and we need look no further for an answer to the question proposed to us. This construction has been adopted in a case recently decided by the Lahore High Court in *Karam Ilahi Muhammad v. Commissioner of Income-tax, Delhi*(2), where the same question arose in a slightly more extreme form and was decided in the same manner.

Our answer to the question referred to us is in the affirmative. The respondent will receive the costs of this application, Vakil's fee Rs. 250. Deposit to be returned. O. P. 16 is not pressed and is dismissed with costs. Vakil's fee Rs. 100.

(338) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvven and
Mr. Justice Pakenham Walsh.*

(23rd October, 1929).

S. M. Perianna Pillai

Assessee.*

v.

The Commissioner of Income-tax, Madras

Referring Officer.

Indian Income-tax Act, (XI of 1922), Secs. 23 (2) and 63—Notice to produce evidence—Assessee applying for adjournment—Powers of adjournment of Income-tax Officer—Communication of adjournment, mode of—If a notice or a requisition under the Act.

Where an assessee applies by post or by telegram for adjournment of an enquiry in respect of which he has been required by a notice under section 23 (2) of the Income-tax Act to produce evidence, the letter or telegram intimating the fact of adjournment granted by the Income-tax Officer is not a notice under section 23 (2) of the Income-tax Act or a requisition within the meaning of section 63 of the Act.

An Income-tax Officer has power to adjourn an enquiry under section 23 of the Income-tax Act.

Case [O.P. No. 77 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble Judges of the High Court under section 66 (2) of the Income-tax Act, 1922.

2. The petitioner is an assessee on the file of the Income-tax Officer, Trichinopoly, Second Circle. For the assessment of the year 1928-29, he submitted a return of his income on the 19th June, 1928. On the 22nd September,

* (1930) 58 M.L.J. 10; 31. L.W. 78; A.I.R. (1930) Mad. 118.

(1) 1 I. T. C. 278.

(2) 3 I. T. C. 456.

1928, the Income-tax Officer served upon him a notice under sections 23 (2) and 22 (4) of the Act calling upon him to produce on the 4th October, 1928, certain accounts and the evidence that he had in support of his return. On the 3rd October, 1928, the petitioner sent the following telegram to the Income-tax Officer: "Tomorrow my family Puja at Palni. Praying adjournment two weeks". The Income-tax Officer granted time till the 12th October, 1928, and sent intimation of the adjournment by ordinary post to the usual address of the petitioner. The petitioner did not appear on the 12th October and the Income-tax Officer accordingly made the assessment to the best of his judgment under section 23 (4).

3. The petitioner thereupon submitted a petition to the Income-tax Officer under section 27 of the Act stating that he left his village on the 3rd October with all the members of his family and returned only on the 16th October, and that on opening the outer door of his house he found inside the house the postcard communicating to him the grant of time till the 12th October. He therefore claimed that he had been prevented by sufficient cause from complying with the terms of the postcard and asked for the cancellation of the assessment. In the course of the enquiry which the Income-tax Officer made on this petition it was admitted that the petitioner had not left his address at the office or made any arrangements to acquaint himself with what orders might have been passed on his request. The postcard sent by the Income-tax Officer was sent to the petitioner's usual address and it admittedly reached him at that address. The Income-tax Officer considered that as the petitioner had taken no steps to inform himself of the orders that might have been passed on his request for an adjournment and had placed himself out of communication by his own default he could not claim to have been prevented by sufficient cause from complying on the date to which the enquiry had been adjourned with the notice served on him under sections 23 (2) and (22) 4. He accordingly declined to re-open the assessment. A copy of his order is appended marked Exhibit A.*

4. The petitioner appealed to the Assistant Commissioner against this decision but without success. A copy of the Assistant Commissioner's order is appended marked Exhibit B.*

5. The petitioner has now asked me to refer to the High Court under section 66 (2) the question of law as to whether the assessment made by the Income-tax Officer is illegal and void. The petitioner points out that the default on account of which assessment had been made under section 23 (4) was the failure to appear and produce accounts on the adjourned date, viz., the 12th October, 1928. His arguments are (1) that the postcard communicating the grant of this adjournment should itself be taken to be the notice under section 23 (2) (the fact that the original notice was under section 22 (4) as well as under section 23 (2) may for the moment be ignored as default in compliance with notice under either entails assessment under section 23 (4)), (2) that it should therefore have been served on the petitioner by registered post and (3) that as the postcard was not sent by registered post there was no valid service of the notice to justify an assessment under section 23 (4). I accordingly refer the following question for the decision of their Lordships:—"Where an assessee applies for adjournment by post or by telegram of an enquiry in respect of which he has been required by a notice under section 23 (2) to produce evidence and the Income-tax Officer grants an adjournment, is the letter (or the telegram where it is a telegram) intimating the fact of the adjournment to the assessee either a notice under section 23 (2), or a requisition within the meaning of section 63 of the Act".

6. Section 63 of the Act says that a notice or requisition under this Act may be served on the person therein-named either by post or, as if it were a summons issued by a Court, under the Code of Civil Procedure, 1908. Assessee usually apply for adjournment either in person or by representative or by written communications (including telegrams). In the first two classes of cases when the Income-tax Officer grants an adjournment he merely informs the party of the fact. He serves no fresh notice under section 23 (2) and the notice continues in operation. Where the application is from an assessee who is not present in person or by representative and made by letter or telegram the Income-tax Officer is not, strictly speaking, bound to take any notice of it. The application being no compliance with the notice under section 23 (2) the party must be held to have committed default; and, in fact, in cases where the Income-tax Officer decides not to grant any adjournment the assessment is sometimes made at once under section 23 (4). But in order to minimise inconvenience the custom has grown up, unlike in Civil Courts, of taking such requests from absentees into consideration and, where an adjournment is granted, of replying to the assessee to that effect. The reply is treated just like ordinary correspondence and is not sent by registered post. Such a letter is, in my opinion, in no sense a notice or a requisition such as is required under section 63 to be served on the party by registered post, or as if it were a summons issued under the Code of Civil Procedure, 1908. I consider that in these cases the duty rests on the assessee of taking steps to inform himself of the result of his application. The mere despatch of an application for time does not amount to a compliance with the notice under section 23 (2) and cannot throw upon the officer the duty of serving a fresh notice on the assessee. That this is so is clear from the fact that when the adjournment is not granted the Income-tax Officer can proceed (as he sometimes does) to make an assessment straight away under section 23 (4); and that when an application is made in person and orders are passed orally, the oral order does not obviously amount to a fresh notice or requisition capable of being served as prescribed in section 63.

My opinion therefore is that the question should be answered in the negative.

T. R. Venkatarama Sastri, M. Subbaraya Aiyer and M. S. Vaidyamatha Aiyer, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

CURGENVEN, J.:—In this case the Commissioner of Income-tax refers the following question for the decision of this Court:—"Where an assessee applies for adjournment by post or by telegram of an enquiry in respect of which he has been required by a notice under section 23 (2) to produce evidence and the Income-tax Officer grants an adjournment, is the letter (or the telegram, where it is a telegram) intimating the fact of the adjournment to the assessee either a notice under section 23 (2), or a requisition within the meaning of section 63 of the Act?"

To understand precisely the nature of this question, it is necessary to look at the circumstances out of which it arose.

The assessee made his return on 19th June, 1928, and on 22nd September a notice under sections 23 (2) and 22 (4) was issued to him requiring him to produce his accounts on 4th October. On 3rd October he sent a telegram pleading a private engagement and asking for an adjournment for two weeks.

If this had been granted in full it would have entailed a postponement of the hearing until 18th October. The Income-tax Officer did not grant it in full but he did adjourn the case until the 12th. This he intimated to the assessee by means of a postcard despatched on the 4th. The assessee did not appear or cause the production of his accounts on the 12th, and since he had thereby failed to comply with the terms of the notice the Income-tax Officer under section 23 (4) made the assessment to the best of his judgment.

The argument addressed to us upon these facts by Mr. T. R. Venkatarama Sastri may be set forth as it stands in the Commissioner's letter of reference:— (1) that the postcard communicating the grant of the adjournment should itself be taken to be the notice under section 23 (2), (the fact that the original notice was under section 22 (4) as well as under section 23 (2) may for the moment be ignored as default in compliance with notice under either entails assessment under section 23 (4)), (2) that it should therefore have been served on the petitioner by registered post, and (3) that as the postcard was not sent by registered post there was no valid service of notice to justify an assessment under section 23 (4).

It might reasonably have been inferred, from the language of the question, that the power of the Income-tax Officer to grant an adjournment was to be presumed; but in fact this line of reasoning is founded upon a denial that he has, at least in circumstances such as the present, any such power. Not having it, it is said that his only course, when he desires to intimate to an assessee a change of date of hearing, is to issue a second notice in terms of the first (save as regards date) in accordance with the theory that the first notice becomes null and void so soon as the original date of hearing is past. Accordingly unless the postcard in the present case can be regarded as a notice under section 23 (2)—which it clearly is not—the assessee received no such notice as he was obliged to comply with. It is sought to qualify the rigidity of this doctrine by the application of the theory of waiver. If the assessee allows his case to be adjourned to an agreed date, he cannot afterwards be heard to contend that he received no valid notice for that date.

I can discover no sufficient ground for denying to an Income-tax Officer the power of adjournment, independently of the doctrine of waiver. Section 23 (3) appears to contemplate it when it says "On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be" and I can find no justification for restricting the latter words to any particular stage of the inquiry. It may be that the mode of expression used in section 23 (3) is not so fully proof against criticism as the language, for instance, of section 31 (1) relating to appeals, where it is said that the Assistant Commissioner "may from time to time adjourn the hearing". But if the Income-tax Officer, as is suggested, has no option but to hear the case "on the day specified in the notice", failure to do so rendering the notice inoperative, the words "as soon after as may be" are irreconcilable with the intention of the Act.

Apart from the presence of these words, I think that the power of an Officer entrusted with an inquiry to adjourn his proceedings, as occasion requires, is so necessary, convenient and universally conceded that unless it is expressly withheld by statute or rule having the force of law it must be taken to vest in him. It is not possible to regard a question of this kind apart from considerations of practical expediency in its relation to the transaction of public business; and it seems scarcely credible that the legislature which may be supposed to have kept such considerations in view, would have intended to place this constraint upon an executive officer in the disposal of his work.

Accepting then that a hearing under section 23 (3) may be adjourned, it follows that no second notice under section 23 (2) for the adjourned date was required by law; and this in effect answers the first part of the question. Mr. Venkatarama Sastri based his case entirely upon this position, but the question put to us also enquires whether the letter or telegram replying to the application for adjournment is a requisition within the meaning of section 63 of the Act. Under section 63 (1) "A notice or requisition under this Act may be served on the person therein-named either by post or, as if it were a summons issued by a Court, under the Code of Civil Procedure, 1908". Under section 27 of the General Clauses Act, if such document is sent by post, it must be registered. The question is whether, in the circumstances stated, an unregistered communication will suffice.

So far as the express terms of the Income-tax Act go, there is no provision either for the manner in which an application for an adjournment should be made or for the manner in which it should be replied to. It cannot therefore be said that any reply sent is a "notice or requisition under the Act" in the sense that the notice prescribed by section 23 (2) is "a notice under the Act", i.e., such as the Act requires to be served upon an assessee. Accordingly, no statutory obligation lay upon the Income-tax Officer to issue any reply. He could have proceeded—it is not denied—to dispose of the case on the 4th October under section 23 (4). If he decided to put off disposing of it until the 12th it was open to him to do so. But, even so, I cannot discover that the assessee had any legal right to a communication appraising him of the fact. It is not the practice, much less a rule of procedure, even in a court of justice that an adjournment date is so intimated to an absent party. No doubt if a party chooses to apply, in person or by representative, at the court or office he can learn what orders have been passed. But he cannot insist upon a telegram or a letter by post, any more than he can insist upon a letter by special messenger. Accordingly I think that the postcard sent to the assessee in this case was not dictated by the terms of the statute but was merely an act of consideration and supererogation the omission of which would have entailed no legal consequences. Upon this view it cannot be held that it amounted to a "requisition under the Act".

I reach this conclusion with the less hesitation because I cannot avoid the apprehension that if it were necessary to hold that the reply to a postal application for an adjournment must be by registered post a quite natural consequence would be a refusal on the part of Income-tax Officers to entertain any such applications to the detriment rather of the assessee than of the officer. Something has been said in the course of the arguments about the requirements of natural justice, as applied to the proceedings of public officers and upon this topic the observations of Lord Haldane, L. C. and of Lord Shaw of Dumfermline in *Local Government Board v. Aldridge* (1), are not inapposite. I quote from the latter's judgment: "The words 'natural justice' occur in arguments and sometimes in judicial pronouncements in such cases. My Lords, when a central administration board deals with an appeal from a local authority it must do its best to act justly, or to reach just end by just means. If a statute prescribes the means it must employ them. If it is left without express guidance it must still act honestly and by honest means. In regard to these certain ways and methods of judicial procedure may very likely be imitated; and lawyer-like methods may find especial favour from lawyers. But that the judiciary should presume to impose its own methods on administrative and executive officers is a usurpation. And the assumption that the methods of natural justice are *ex necessitate* those of Courts of Justice is wholly unfounded."

Where an executive officer, or a department of Government supplements the procedure laid down by statute, the principles formulated in this quotation afford a test whether the supplementary procedure is in accordance with natural justice and will not be interfered with. I think that the procedure in the present case answers to this test.

I would answer both branches of the question put to us in the negative. The petitioner will pay the Commissioner's costs. Advocate's fee Rs. 250.

PAKENHAM WALSH, J.:—This is a question referred by the Income-tax Commissioner under the following circumstances: The assessee submitted on 19—6—1928, a return of his income. On 22—9—1928 the Income-tax Officer served on him a notice under Secs. 23 (2) and 22 (4) of the Act calling upon him to produce on 4th October, 1928, certain accounts and the evidence he wished to rely on in support of his return. On 3—10—1928 the assessee sent the following telegram to the Income-tax Officer. "Tomorrow my family Puja at Palni. Praying adjournment for two weeks." The Income-tax Officer gave an adjournment till 12—10—1928, sending the intimation by ordinary post. The assessee did not appear on 12—10—1928, and the Income-tax Officer made the assessment to the best of his judgment under section 23 (4). The assessee then moved the Income-tax Officer under section 27 of the Act to cancel the assessment. He alleged that he returned with his family to his house only on 16—10—1928, when he found the post card there intimating the adjournment to 12—10—1928. In the course of the enquiry it was admitted that the assessee had not left any address at the office, nor made any arrangements to acquaint himself with any orders that the Income-tax Officer might pass on his telegram for adjournment. The postcard had been admittedly delivered at the assessee's usual address and in good time to acquaint him with the adjournment. The Income-tax Officer held that the assessee had placed himself out of communication by his own default and declined to reopen the assessment. An appeal against this decision to the Assistant Commissioner proved unsuccessful. The assessee then argued before the Commissioner: (1) that the postcard communicating the grant of adjournment should itself be taken to be a notice under section 23 (2), (2) that it should therefore be served on the assessee by registered post, (3) that as the postcard was not sent by registered post there was no valid service of the notice to justify an assessment under section 23 (4). The Commissioner has accordingly referred the following question to the High Court: "Where an assessee applies for adjournment by post or by telegram of an enquiry in respect of which he has been required by a notice under section 23 (2) to produce evidence, and the Income-tax Officer grants an adjournment, is the letter (or the telegram where it is a telegram) intimating the fact of the adjournment to the assessee either a notice under section 23 (2) or a requisition within the meaning of the Act?"

Section 63 (1) reads "A notice or requisition under the Act may be served on the person therein named either by post or as if it were a summons issued by a Court under the Code of the Civil Procedure 1908". It is not denied that if this was a notice or a requisition under the Act it must be sent by registered post and if it were at the same time a notice under section 23 (2) and not so sent the Income-tax Officer could not in default of the assessee's appearance proceed to make an assessment to the best of his judgment under section 23 (4). The second question as propounded becomes unnecessary if the first is answered in the negative. It is clear that a notice under section 23 (2) is necessarily also a requisition since the party is either required to attend in person or to produce his books or, as the notice form shows, to do both.

If a notice or requisition is issued under any other section, then though it may be necessary under the terms of section 63 to send it by registered post, the failure to do so would not affect the power of the Income-tax Officer to act under section 23 (4). I take it therefore, specially reading it with the arguments of the assessee set out by the Commissioner as the basis of his question, that the question before us really is this: Where an assessee applies for adjournment by post or by telegram of an enquiry in respect of which he has been required by a notice under section 23 (2) to produce evidence and the Income-tax Officer grants an adjournment, is the letter (or the telegram where it is a telegram) intimating the fact of the adjournment to the assessee either a notice or a requisition under 23 (2)? If it is held to be so, it will of course attract the terms of section 63 (1) and if it is not so, while it might still attract the terms of section 63 (1), it would be no ground for objecting to an assessment under section 23 (4) in default of the assessee's appearance on the adjourned date, that the terms of section 63 had not been complied with.

The argument of the learned pleader is briefly this: If on the day appointed for the enquiry the assessee is absent or fails to comply with all the terms of the notice issued under section 23 (2) the Income-tax Officer must at once proceed to assess him under section 23 (4) or if he does not do so, but intimates to him a fresh date of hearing, he must issue to him a fresh notice under section 23 (2). In fact he would go so far as to deny the Income-tax Officer any inherent power of adjournment in cases where the assessee fails to appear even though the assessee should have asked for such adjournment himself (unless he complies with the date asked for by the assessee) and would read that part of section 23 which runs "On the day specified in the notice issued under sub-section 2, or as soon afterwards as may be, the Income-tax Officer, after hearing such evidence as such person may produce.....shall by an order in writing assess the total income of the assessee", as if the words ran "On the day specified in the notice issued under sub-section (2) or, *provided the assessee has appeared in compliance with the terms of the notice* as soon afterwards as may be", etc.

Now it would require very strong reasons to read into a section words like these which are not there and which deny to the Income-tax Officer a very ordinary and necessary power of granting adjournment even though the assessee may not have appeared or complied with the notice issued under section 22. To support this contention he argues that in section 23 (4) there is no allusion to any adjourned date. Apart from that being a very slight ground to read into section 23 (3) words which are not there, it has been pointed out for the Crown that section 23 (4) read with section 23 (2) shows clearly that the penalty of an assessment under section 23 (4) (which for the sake of convenience, though not quite accurately may be called a random assessment) need not necessarily be imposed the moment the default is committed. One of the defaults entailing a random assessment under section 23 (4) is failure to make a return under sub-section 1 of section 22, but sub-section 3 of section 22 provides that if the assessee having failed to submit a return, or having found an omission or error in his return furnishes a return or a revised return as the case may be *at any time before the assessment is made*, any return so made *shall be deemed to be a return* made in due time under this section. Hence though section 23 (4) does not mention any adjourned date, section 22 (3) lays down that there is a *locus penitentiae* right up to the time when the actual assessment is made. No argument therefore can be drawn from the wording of section 23 (4) to support the introduction of such words under section 23 (3) as would deprive the Income-tax Officer of the power of granting an adjournment in case the assessee had not complied with the terms of the order under section 23 (2).

The argument in the circumstances of the present case implies a further fallacy. The Income-tax Officer having granted an adjournment there was no default by the assessee on 4—10—1928 when he did not appear. The Income-tax Officer could not therefore on any fair or judicial principles of procedure have visited him with the penalty of an assessment under section 23 (4) for his non-appearance on that date. If that is so, where was the point at which the Income-tax Officer had to start proceedings all over again under section 23 (2)? Obviously this occasion could not, on the argument, have arisen till the assessee absented himself on 12—10—1928 but the basis of the learned Advocate's argument is that the notice intimating the adjournment to the 18th October, was the fresh notice under section 23 (2) which required registration. It may be thought that to deny the Income-tax Officer a power of adjournment in cases where the assessee is absent, and even though the latter asks for it, is going further than is necessary to prove the assessee's contention in this reference, but I think the learned Advocate is quite correct in arguing for this extreme position and that it is really essential to his plea; for, otherwise, the obvious answer that there is no necessity at all for the Income-tax Officer to send any reply to a letter or telegram asking for adjournment is almost fatal to his case. It has not, and cannot be, contended that any such duty of reply is cast on the Income-tax Officer, nor can it be denied that if he has a power of adjournment he may whether, to suit his own convenience or that of the assessee, simply write on the file 'adjourned to such and such a date', or post it on the board (if such a board is kept). Such an endorsement on the file or notice on the board he is not bound to communicate to the assessee if the latter is absent. It is for the assessee to bestir himself and make enquiries, or to look on the notice board or elsewhere. If this is so—and it cannot, I consider, be controverted—then the Income-tax Officer is neither bound to proceed under section 23 (4) on the original date of hearing, nor to begin matters all over again by fresh notice under section 23 (2) so that really the two arguments that he has no power of adjournment if the assessee does not appear and the corollary that he must either act at once under section 23 (4) or begin with a fresh notice under section 23 (2) are absolutely essential to establish the contention that a notice of adjournment is a notice under section 23 (2). I consider that the assessee has failed to make out either of these preliminary contentions.

In my view and for the determination of the case it is not material to decide whether a notice or a requisition, if it is not one under section 23 (2), has to be registered. By the terms of section 63 if the notice is one under the Act it clearly must be registered, but if it is not a notice under section 23 (2) the failure to do so will not make an assessment under section 23 (4) invalid. That is why that part of the reference question which asks whether the letter in this case is a requisition under section 63 has no bearing on the matter before us if the answer to the first question be in the negative. It raises a question with which we are not concerned. If I had to decide it I should say that it is not a notice under the Act at all. Again on the abstract and academic question whether a notice of adjournment made on the request of the assessee is a mere notice or is also a requisition (which question really does not arise in this case) I do not feel bound to give an answer, once it is found that it is not a notice or requisition under section 23 (2). If I had to express an opinion I should say that it must necessarily be a notice (by which, I take it, is meant an intimation which brings something to somebody's notice). I doubt that it is a requisition because a party is supposed by the original summons or notice to go on appearing till his case is finished, whether this is explicitly so stated in the original summons or not. Any other construction would mean that the assessee would have complied with the original summons in this case if he had merely

gone to the office on the day in question, flung his books down before the Income-tax Officer and walked off. The words "attend at my office" must surely mean more than this and must mean "attend for as long as I shall require you on that day and also attend in the same way on subsequent dates to which the case may be adjourned." But in fact nothing turns here on whether the post card was a notice or a requisition or a notice *plus* a requisition. If it was any of these things and was issued under section 23 (2), then the assessee's contention is correct. If it was not issued under section 23 (2), it does not affect the question of the right of the Officer in case of default to proceed under section 23 (4).

Again I do not feel myself bound to deal with a case where an assessee attends on the due date and finds that the Income-tax Officer is not sitting, and has fixed no date of adjournment. Such conduct by the Income-tax Officer would, unless unavoidable, be a clear dereliction of his duties. I am rather inclined to think that if there were such a dereliction, or if by *force majeure*, say a sudden accident to the Income-tax Officer which incapacitated him from giving directions, or his sudden death, the enquiry were left in the air on the day fixed for it, it might very well be that proceedings would have to begin all over again. The Act does not expressly provide for any such break in the enquiry. A question of this sort may be decided when and if it arises. It is not before us to decide.

Although the contention in the present case is purely one of law, it is quite clear that if the assessee's argument is accepted that every notice of an adjourned date even if made at the petitioner's request (if it is not the date required by the petitioner) necessitates a fresh registered notice under section 23 (2), the result will simply be in practice that all such adjournments will be refused and the assessment will be decided under section 23 (4) forthwith. That will work as a great hardship to assessees. The grant of an adjournment is a concession. It was argued that it is no concession if the date asked for by the assessee is not granted. I dissent entirely from this view. The request for an adjournment in these cases implies *prima facie* a request that the right to make an assessment under section 23 (4) shall not be exercised. The mere granting of this is a great concession. Then the petitioner's wishes as regards the adjourned date are met partly though not in full. Let us suppose a telegram or letter for adjournment received as in this case either on the day before the hearing or on the date of hearing. The Income-tax Officer is not able to adjourn the enquiry for as long as the assessee wishes. He can grant an adjournment to the next day or the day after, but a registered letter, even if posted at once, cannot reach the assessee in time. In such cases on the contention raised he must refuse even the shorter adjournment which he was prepared to grant or else start proceedings all over again.

It is also quite clear if the petitioner's contention is correct, the registered notice of adjournment must not only intimate the adjourned date but an entirely fresh list of the other documents or evidence required (admittedly joint notices under sections 22 (4) and 23 (2) are legal and the notice in this case is such). If the Income-tax Officer does not go to all this trouble, it will not be a valid notice. The facts in the present case make this clear. The assessee must and does contend that even if he had got and read the post card in time to attend the hearing on the 12th, he would not have been bound to attend it as the notice was not registered. So that even knowledge gained from a notice to him by the Court itself would not make the notice a valid one. It follows therefore that a mere reference in a fresh registered notice to the evidence required in a previous

notice can and will be equally impugned as not constituting a valid notice of what evidence the assessee is required to produce. *Ex-hypothesi* an entirely fresh proceeding under section 23 (2) has been started and the terms of section 23 (2) must be complied with fully and literally. This will certainly not be an inducement to the Income-tax Officers to spend trouble, time and money in granting requests by post or wire for adjournments which they are admittedly not bound to notice or answer at all.

A decision in *In the matter of Lachhman Das Babu Ram*(1), has been referred to by the learned advocate for the assessee. I do not think it has any bearing on this case. It was held there that if the Income-tax Officer during an enquiry under section 23 (3) required more evidence he can call for it, and it might be advisable to do so by a fresh notice under section 23 (2). Now it is clear that such notice would be only one supplementary to the one already sent and it need not contain the particulars already given in the previous notice. To hold that a supplementary notice can be sent under section 23 (2) when the Income-tax Officer requires fresh evidence is a very different proposition from holding that a notice, which the Income-tax Officer need not send at all, intimating an adjournment made on a letter or telegram by the assessee asking for it, is a fresh notice or even a supplementary notice under section 23 (2).

I would answer the question (in the form in which I understand it is really intended to be put) thus: That where an assessee applies for adjournment by post or by telegram of an enquiry in respect of which he has been required by a notice under section 23 (2) to produce evidence and the Income-tax Officer grants an adjournment, the letter (or the telegram where it is a telegram) intimating the fact of the adjournment to the assessee is neither a notice nor a requisition under section 23 (2) and does not affect the power of the Income-tax Officer to assess under section 23 (4) if the assessee fails to appear on the date of adjournment or commits any of the other defaults rendering him liable to be assessed under that section.

If an answer has to be given to the second part of the question referred to us I would answer it also in the negative.

KUMARASWAMI SASTRI, J.:—I have had the advantage of reading the judgments of my learned brothers. I agree with them that the answer should be in the negative and have nothing useful to add. The petitioner will pay Rs. 250, Vakil's fee to Commissioner.

(339) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Justice Sir Kumaraswami Sastri, Kt., Mr. Justice Curgenvven and
Mr. Justice Pakenham Walsh.*

(23rd October, 1929).

T. M. M. Sankaralinga Nadar and Brothers	...	} Assesseees *
T. M. P. Sankaralinga Nadar and Brothers	...	
T. M. S. Madalai Nadar and Brothers	...	

vs.

The Commissioner of Income-tax, Madras .. Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 22 (4) and 37—Income-tax authorities, if Courts—Res judicata, applicability of the doctrine of—Principles

(1) 2 I.T.C. 1.

* (1930) I. L. R. 53 Mad. 420; 58 M. L. J. 260; 31 L. W. 739; A. I. R. (1930) Mad. 209

governing enquiries by Income-tax authorities—Decision of Income-tax Officials, when can be re-opened by succeeding officer—Power to call for accounts more than 3 years old—Adverse inference on non-production—Indian Evidence Act, Sec. 114.

An Income-tax Officer proceeding to assess the income of an assessee after making an enquiry as contemplated by the Income-tax Act is not a court governed by the doctrine of res judicata applicable to the decisions of Civil Courts. In conducting the enquiry he has to act judicially and to exercise his discretion not capriciously but on recognised judicial principles.

Where Income-tax Officials after enquiry allowed the assessee to claim a deduction as for interest paid on sums of money alleged to be the stridhanam monies of his female relations lent to him, a succeeding Officer is entitled to re-open the question of the alleged loan, if fresh facts come to light which on an investigation will entitle the Officer to come to a different conclusion.

The proviso to Sec. 22 (4) limits the power of the Income-tax Officer to call for accounts for more than three years prior to the previous year when the Officer proceeds to make the assessment to the best of his judgment under Sec. 23 (4). There is nothing to prevent the Income-tax Officer making an enquiry as regards the truth or otherwise of the allegations of the assessee in his return, from requiring the assessee to produce any evidence including accounts more than three years old and on non-production, from drawing an adverse inference under section 114 of the Evidence Act.

Cases [O. P. Nos. 175 to 178, 229 and 253 of 1928], stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, in compliance with the orders of the High Court.

CASE.

[O. P. Nos. 177 & 178 of 1928].

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Income-tax Act (XI of 1922).

2. The petitioners are a Hindu undivided family doing business in Virudhunagar in the Ramnad district within the jurisdiction of the Income-tax Officer, Sattur (now Virudhunagar).

3. In the course of the assessment proceedings for 1926-27 the petitioners claimed to deduct the following sums in computing their income from business: (i) a sum of Rs. 22,239 said to be interest on the moneys alleged to have been borrowed; (ii) a sum of Rs. 12,809 as bad debts, and (iii) a sum of Rs. 1,370 being the amounts collected and paid on account of Mahimai.

4. The facts with regard to these claims are as follows:—

(i) The petitioner's books showed their own capital as about Rs. 2½ lakhs and an almost equal sum as having been borrowed for the purposes of the business from certain of their female relatives. Interest amounting to Rs. 22,239 on these alleged borrowings was claimed as a deduction. The Income-tax Officer wished to satisfy himself that these large sums of capital had really been borrowed and were not moneys belonging to the family as such. He called on the petitioners' auditor to produce evidence from the earlier accounts in support

of their claim that the so-called borrowed capital amounting to over Rs. 2 lakhs was actually Stridhanam property of the ladies concerned. The auditor replied that he had examined the books of the past 4 or 5 years and found that these moneys had been brought forward from years prior to that. He also alluded to the fact that these items of borrowed capital had been accepted as such by previous Income-tax Officers. The Officer was not satisfied with this. He held that the evidence on which previous Income-tax Officers had acted was not sufficient to establish the fact claimed. He thereupon issued a summons under section 37 calling for the production of the accounts of the years from 1917 to 1920. In reply to this the petitioners stated that the accounts called for "have been mislaid and are not forthcoming". The Income-tax Officer did not consider it likely that these accounts had been destroyed, or that they could not have been produced if the petitioners had been minded to do so; and it may be mentioned here that one of the petitioners, T. M. M. Sankaralinga Nadar, admitted in the course of a subsequent enquiry that it was not their custom to destroy old ledgers and day-books. The petitioners had now been given several opportunities of satisfying the Income-tax Officer on the point in dispute and the Officer was still not satisfied. From the petitioners' failure to produce the old accounts specifically called for he drew the inference that the evidence of the accounts would have been unfavourable to the petitioners. The Income-tax Officer therefore disallowed the deduction claimed.

(ii) The sums claimed as bad debts consisted of two items, one Rs. 1,329 and the other Rs. 11,480. The Income-tax Officer wished to satisfy himself on the two essential points which have to be examined in such cases, viz., that the debts had arisen in the course of business, and that they were irrecoverable. He therefore called on the petitioners to prove the origin of these debts. The petitioners pleaded their inability to prove the origin of these debts but claimed that if a debt be entered in the accounts and subsequently written off it should be allowed without further question. The Income-tax Officer was not prepared to allow the deduction without satisfactory proof. His finding was (1) that the petitioners had not proved that these debts arose in the ordinary course of business and (2) that the sum of Rs. 11,480 at any rate had not become irrecoverable (the petitioners themselves having admitted that they had obtained an acknowledgment from the debtor in the year preceding the year of account and that they were demanding payment from him). He therefore disallowed these claims with the exception of a sum of Rs. 2,592 included in the debt of Rs. 11,480 which he allowed as representing interest due from the debtor which had been included in the assessments in previous years.

(iii) The Income-tax Officer found that sums credited in the Mahimai account represented either recoveries made by the petitioners from customers as part of the sale price of goods sold by them, or amounts which though debited in the purchase accounts as part of the purchase price of articles had not really been spent on the purchase of goods or on any other purpose connected with the business. He therefore considered that the recoveries from the customers must be regarded as part of the petitioners' business receipts and that the amounts debited to the petitioners' purchase accounts could not be regarded as expenditure incurred for the purpose of earning their profits. He accordingly included the collections in the assessment and declined to allow as deductible expenditure the amounts debited to "Purchases" on this account. A copy of the Income-tax Officer's order is filed marked Exhibit A.*

5. The petitioners appealed to the Assistant Commissioner against the disallowance of these sums. The Assistant Commissioner gave another opportu-

nity to the petitioners to prove in regard to item (I) that the sums in question were Stridhanam moneys, and in regard to item (II) that the debts were trade debts and had really become bad. The petitioners again failed to take advantage of the opportunity given to substantiate their claims, by production of the old accounts. In regard to the claim to deduct interest paid on the alleged Sridhanam moneys the Assistant Commissioner also observed that the capital which was admitted by the petitioners to be their own was shown under 13 different ledger heads, a fact which indicated that it was the practice of the petitioners to show their capital in the names of the various members of their family. The Assistant Commissioner therefore confirmed the Income-tax Officer's orders on these points. He also agreed with the Income-tax Officer's decision regarding item (iii). In regard to item (ii)—Bad debts—the Assistant Commissioner further considered that the Income-tax Officer was wrong in having allowed the sum of Rs. 2,592 referred to in paragraph 3 (ii). He accordingly enhanced the petitioner's assessment by this amount. A copy of his order is filed marked Exhibit B.*

6. The petitioners appealed to me against the enhancement made by the Assistant Commissioner and at the same time put in a petition asking me to refer certain questions of law to the High Court. I rejected both the appeal and the application for a reference to the High Court for the reasons set out in my order marked Exhibits C* and D*.

7. The petitioners thereupon moved the High Court under section 66 (3) of the Income-tax Act and the High Court has by its order dated 12th March, 1929, directed me to state a case on the following questions:—

- (a) Whether when in a previous year of assessment a decision was arrived at after investigation and enquiry that certain amounts standing in the name of certain ladies in the petitioners' accounts, were the Stridhanam amounts belonging to them and as such the interest paid in respect of the said amounts was held to a valid deduction, it is open to the Income-tax authorities to re-open the question of the ownership of the amounts in a subsequent year of assessment and whether the authorities are not barred by principle of *Res Judicata* or otherwise from reopening the said question.
- (b) Whether when amounts are shown in the account books as the amounts belonging to certain ladies of the family and the Income-tax authorities have treated the said amount for several years as such and when they have assessed the ladies separately in respect of the said amount on that basis, it is competent for the authorities to levy assessment in respect of the very same amount on the petitioners, the assessment on the ladies having become final not having been set aside by appropriate proceedings.
- (c) Whether in the absence of any affirmative evidence on the part of the Crown it is open to the authorities to presume that the amount standing *prima facie* in the name of the ladies belonged to petitioners.
- (d) Whether there was any legal evidence before the Income-tax Officer and Assistant Commissioner in support of their findings as to the ownership of the said amounts.
- (e) Whether there is any jurisdiction for the Income-tax authorities purporting to act under section 37 of the Act to call upon an

* Not Printed.

assessee to produce accounts relating to a period prior to three years of assessment and whether any inference can be drawn against the assessee by reason of non-production thereof of such accounts.

- (f) Whether when goods are sent to an assessee for the purpose of sale on commission and a certain small amount is charged on the consignor for each bag sent as and for Mahimai which is paid over by the assessee either immediately or subsequently to the trustees of the Mahimai fund intact, the said amount is liable to be assessed for income-tax.
- (g) Whether when debts are actually written off by the assessee as an irrecoverable bad debt it is open to the authorities to disallow a deduction in respect of the same on the ground that the origin of the debt has not been proved.

8. My opinion on the above questions is as below:—

Question (a). This question contains an initial mis-statement of fact. It is not correct to say that in a previous year of assessment a decision was arrived at, after investigation and enquiry, that certain amounts standing in the name of certain ladies were Sridhanam amounts belonging to them. I have gone through the records of the case carefully and I do not find any material to warrant this statement. What the Income-tax Officer did in that year, was merely to accept a statement made by the petitioners supported by affidavits that these were Stridhanam amounts and make the assessment on that basis. The contention of the petitioners that the Income-tax Officer was bound to follow the decisions come to in previous assessments proceeds on the mistaken assumption that there was an investigation or a decision. Even assuming that there had been a decision arrived at (which as I have shown above there had not) I am unable to agree with the petitioners' argument that the question could not be examined again. It was the Income-tax Officer's duty to set at rest his doubts concerning the genuineness of any claim made before him. If the evidence on record relating to previous assessments had been sufficient to clear those doubts he would doubtless have acted upon it. This was evidently not the case and in such circumstances I am of opinion that there was nothing to prohibit him from calling upon the petitioners to produce evidence of facts that they desired to establish.

Question (b). It is true that at the time when the assessment was made on the petitioners the sum alleged to have been paid as interest had already been assessed in the hands of the alleged recipients but as I find that the assessments made on the ladies have since been cancelled and the tax refunded, the question propounded does not arise on the facts of the case.

Question (c). It is obviously impossible to expect an assessing officer to produce affirmative evidence on such a point. When any fact is especially within the knowledge of any person, the burden of proving that fact is upon him. In this case the fact claimed, viz., that the moneys were borrowed, was within the knowledge of the petitioners and the burden of proving that fact therefore lay upon them. They did not produce any satisfactory evidence or discharge this burden. The evidence which the Income-tax Officer considered would have been clear on the point and which it was even indicated to them that they would have done well to produce, viz., the accounts of the years 1917-1920, they failed to produce. The Income-tax Officer was entitled in these circum-

stances to presume that this evidence, if produced, would have been adverse to their claim. He found from the books that the petitioners were in the habit of showing their own capital in the names of various members of the family. In my opinion therefore it was open to the Income-tax Officer to arrive at the conclusion that he did regarding the ownership of the moneys.

Question (d). This question was not raised before me, and appears to be merely a paraphrase of the preceding question. As I have stated in the course of my opinion on that question the petitioners made some claim which they were required to substantiate and if they failed to substantiate it, the assessing officer was entitled to draw his own conclusions. It is impossible for the assessing officer to have "legal evidence" in such cases and in my opinion it is not necessary for him to have it.

Question (e). The issue of a summons under section 37 in this case was quite unnecessary. Under section 23 (3) the Income-tax Officer had power to call for evidence on specified points and he made it very clear to the petitioners that he wanted evidence on the question of the ownership of the sums alleged to be Sridhanam moneys. He went, so far, no doubt, as to specify the kind of evidence that he required, but he also sufficiently indicated that he was prepared to consider any evidence on the point that the petitioners were willing to produce. If satisfactory evidence had been forthcoming I am quite certain that he would not have disallowed the deduction claimed merely on the ground that his summons had not been complied with. At the appeal stage a further enquiry was held under the instructions of the Assistant Commissioner when the petitioners were specifically informed that they might produce "any other evidence which they may have to show that the amounts shown in their books to the credit of the several female members of their family are their own Sridhanam amounts given to them at the time of their marriage or other special occasions". The ground for the decisions come to therefore both in the assessment and appeal proceedings was that the petitioners had been given repeated opportunities of proving certain facts the burden of proving which lay heavily upon them and that they had failed to prove them. The decision would stand on this ground even if the petitioners were right in their contention that the Income-tax Officer had no authority to draw any adverse inference from the non-production of the accounts in question. But I am of opinion that their contention is not correct. The right to draw an inference from the non-production of accounts is based upon ordinary human conduct and the common course of natural events and has nothing whatever to do with the existence or non-existence of a power to compel their production.

Question (f). The Assistant Commissioner has found that the moneys credited to the Mahimai account consisted of (1) amounts collected in certain instances as part of the sale price of goods sold by the petitioners and (2) in other instances amounts debited to the purchases accounts but not actually spent on the purchases of goods or for any other purpose connected with the petitioner's business. The question I am directed to refer for decision has to do only with the collections referred to in item (1). I agree with the Assistant Commissioner's finding and consider that the receipts are taxable as receipts of the business. They undoubtedly form part of the sale price of the goods and are so treated by the persons to whom the goods are sold.

Question (g). This question apparently covers only the sum of Rs. 1,329 referred to in paragraph 4 (ii) above, the main reason for the disallowance of the other sum having been the finding that the debt had not become

irrecoverable. I consider the Income-tax Officer was justified in requiring the petitioners to produce evidence to prove that this sum represented trade outstandings. It is a well known principle of Income-tax practice that in computing the profits of a business a bad debt which has been written off is an allowable deduction only when it is shown that the debt had its origin in the business.

CASE.

[O. P. Nos. 176 and 229 of 1928].

I have the honour to state the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Income-tax Act, XI of 1922.

2. The petitioners are a Hindu undivided family doing business in Virudhunagar in the Ramnad district within the jurisdiction of the Income-tax Officer, Sattur (now Virudhunagar).

3. In the course of the assessment proceedings for 1926-27 the petitioners claimed to deduct the following sums in computing their income from business: (i) a sum of Rs. 26,202 said to be interest paid on moneys alleged to have been borrowed for the business, and (ii) Rs. 3,141 alleged to be interest paid on moneys borrowed from Annadhanam Charity Fund''.

Item (i). The petitioners' books showed their own capital as about Rs. 51,951 and a sum of Rs. 2,72,225 as having been borrowed for the purposes of the business from certain of their female relatives. Interest amounting to Rs. 26,202 on these alleged borrowings was claimed as a deduction. The Income-tax Officer wished to satisfy himself that these large sums of capital had really been borrowed and were not moneys belonging to the family as such. He called on the petitioners' auditor to produce evidence in support of their claim that the so-called borrowed capital amounting to over Rs. 2½ lakhs was actually the Sridhanam property of the ladies concerned. The auditor replied that "the deposits made by the assessee's female members are the Sridhanam amounts of the several female members. Proofs in support of the above were given during the assessment proceedings of the assessee's in 1923-24." The Officer was not satisfied with this. He was of opinion that the evidence on which the previous Income-tax Officers had acted was not sufficient to establish the fact claimed. He therefore called on the petitioners under section 23 (2) to produce evidence in support of their return and at a subsequent stage issued a summons under section 37 specifically requiring the production of their accounts for the years Pingala, Kalayukthi and Sidharthi, roughly the period from 1917 to 1920. In reply to this summons one of the petitioners stated that the "accounts called for pertains to a period for more than three years prior to the accounting year and it is not quite probable to be retained by a man of our type of business". At the same time the petitioners offered to produce affidavits to the effect that the moneys standing to the credit of the ladies in the petitioners' books belonged to them. The Income-tax Officer did not consider such affidavits as sufficient evidence in the absence of corroborative evidence to support them. In view of the failure of the petitioners to produce their old accounts which would show the origin of these moneys he drew the inference that the evidence of those accounts would have been unfavourable to them. He therefore disallowed the deduction claimed.

Item (ii). It was found by the Income-tax authorities in previous years that the amount standing to the credit of the Annadharmam Charity Fund was the petitioners' own money and that no trust had been constituted in respect of that fund. In the course of the assessment for the year 1926-27 the petitioners

claimed that the fund was trust property and in support of their allegation produced a trust deed executed on 1st July, 1925. The Income-tax Officer found that the fund was constituted into a trust on and after the 1st July, i.e., about 10 months after the petitioners' year of account commenced and that prior to that date there was no trust in existence in respect of the fund. He therefore disallowed the interest relating to the period prior to July 1st, i.e., a sum of Rs. 2,762.

4. The petitioners appealed unsuccessfully against these disallowances to the Assistant Commissioner. A copy of the Assistant Commissioner's order is filed marked Exhibit A.*

5. The petitioners thereupon put in an application under section 66 (2) of the Income-tax Act requiring the Commissioner to refer certain questions of law to the High Court and my predecessor rejected the application for the reasons stated in his order filed marked Exhibit B.*

6. The petitioners then moved the High Court under section 66 (3) of the Income-tax Act and the High Court has by its order dated 24th April, 1929, directed me to state a case on the following questions:—

(1) When once it has been decided after due enquiry that amounts of a certain character are not liable to the tax payable by a particular individual and that view has been acted upon for several years, whether the same question can be re-opened for a subsequent year.

(2) Whether an Income-tax authority can call for accounts for a period earlier than three years prior to the year of account.

(3) Whether on the admitted facts of the case the whole of the interest payable to the Annadhanam fund for the year of account is not an admissible deduction under section 10.

Question (1). This question contains an initial mis-statement of fact. It is not correct to say that "it has been decided after due enquiry" that these funds were the Stridhanam property of the female members of the petitioners' family, or that the interest said to have been paid thereon was a proper deduction in computing the business profits of the petitioners. I have gone through the records of the case carefully and I do not find any material to warrant this statement. What the Income-tax Officer did in the year in which the enquiry is said to have been made, viz., the year 1923-24 was to accept certain affidavits filed by those persons that the moneys were their Stridhanam property and make the assessment on that basis. The contention of the petitioners that the Income-tax Officer was bound to follow the decision come to in previous assessments proceeds on the mistaken assumption that there was an investigation or a decision. Even assuming that there had been a decision arrived at (which as I have shown above there had not) I am unable to agree with the petitioners' argument that the question could not be examined again. It was the Income-tax Officer's duty to set at rest his doubts concerning the genuineness of any claim made before him. If the evidence on record relating to previous assessments had been sufficient to clear those doubts he would doubtless have acted upon it. This was evidently not the case and in such circumstances I am of opinion that there was nothing to prohibit him from calling upon the petitioners to produce evidence of the facts that they desired to establish.

Question (2). Apparently the petitioners' contention is that in view of the proviso to section 22 (4) the Income-tax Officer had no power by the issue of

a summons under section 37 to call for the accounts of a year earlier than three years prior to the year of account. The issue of a summons under section 37 in this case was quite unnecessary and when the summons was disobeyed the Income-tax Officer made no attempt to enforce it. Under section 23 (3) the Income-tax Officer had power to call for evidence on specified points and in this case he made it very clear to the petitioners that he wanted evidence on the question of the ownership of the sums alleged to be Stridhanam moneys. He even went so far as to specify the kind of evidence that would be best. The burden of proof in this matter rested on the petitioners and their failure to discharge that burden by the production of the best evidence resulted in the decision going against them. The question whether or not the Income-tax Officer had power to compel the production of any old accounts had nothing whatsoever to do with the correctness of his decision in this matter.

Question (3). The finding in this case is that prior to July 1st, 1925, the amount standing to the credit of the Annadhanam Charity Fund was the petitioners' own money and that there was no valid trust before that date. There is no provision of law that permits a deduction from the profits of the interest paid by the proprietor of a business to himself on capital invested by him in the business. On the finding mentioned above therefore the disallowance made by the Income-tax Officer was quite correct.

CASE.

[O. P. Nos. 175 and 253 of 1928]

I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3) of the Income-tax Act (XI of 1922).

2. The petitioners are a Hindu undivided family doing business in Virudhunagar in the Ramnad district within the jurisdiction of the Income-tax Officer, Sattur (now Virudhunagar).

3. In the course of the assessment proceedings for the year 1926-27, they claimed and were allowed to deduct from their profit a sum of Rs. 23,279 being the interest paid on certain sums alleged to have been borrowed for the purposes of their business credited in the accounts in the names of their female relatives. Later on the Income-tax Officer received information that the sums credited in the accounts in the names of the ladies were the property of the joint family and that the petitioners had escaped assessment in respect of the said sum of Rs. 23,279. He therefore proposed to levy additional tax and issued the notice required by section 34 of the Income-tax Act. The petitioners replied that the amounts appearing in the account books to the credit of the ladies of the family were the separate funds of those ladies and that this fact "had been accepted by successive Commissioners of Income-tax after due enquiry ever since the accounting year, 1920-21". The Officer was not satisfied with this. He considered that the evidence on which the Income-tax authorities had acted, viz., the statement of the managing member of the family was not sufficient to establish the fact claimed. He therefore issued a summons under section 37 and required the petitioners to produce their accounts of the years, Nala, Pingala and Kalayukthi (roughly the period from 1916 to 1919), these being the accounts which he had reason to believe would throw light on the character of the moneys credited in the names of the ladies. The petitioners' Vakil however replied to say that "the assessee objects that he is not liable to be required to produce any accounts relating to a period more than three years prior to the previous year".

The Income-tax Officer thereupon required them under section 23 (3) of the Income-tax Act to produce evidence in support of their allegation that the sums to the credit of the ladies were their separate property and also required them specifically to produce the ledgers of their business containing the folios of the ladies for the three years ending with Adi Kalayukthi (July, 1919). The petitioners did not produce the evidence of the ledgers required by the Income-tax Officer but examined some witnesses on their behalf. The Income-tax Officer refused to place any reliance on the statement of the witnesses which was interested and vague and was not supported by any contemporaneous record. In view of the failure of the petitioners to produce their old accounts which would show the origin of these moneys he drew the inference that the evidence of those accounts would have been unfavourable to them. He therefore made the additional assessment as proposed. A copy of the Income-tax Officer's order is filed marked Exhibit A.*

4. Against this assessment the petitioners appealed unsuccessfully to the Assistant Commissioner. A copy of the order of the Assistant Commissioner is filed marked Exhibit B.*

5. The petitioners thereupon submitted an application asking the Commissioner to refer certain questions of law to the High Court. My predecessor rejected the application for the reason stated in his order filed marked Exhibit C.*

6. The petitioners thereupon moved the High Court under section 66 (3) of the Income-tax Act and the High Court has by its order quoted above directed me to state a case on the following questions:—

(1) Whether the decision of the Board of Revenue in I. T. A. No. 0/20-21, dated 11th June, 1921, as to the ownership of separate property by (1) The applicant's mother, (2) The applicant's wife, (3) The applicant's brother Muthu Nadan's wife and (4) The applicant's brother Dhanakoti Nadan's wife, does not constitute the question of such separate ownership *res judicata* and estop the income-tax authorities from re-opening that question in a subsequent year.

(2) Does not the decision of the Commissioner of Income-tax in I.T.R. No. 155/24-25, dated the 27th May, 1925, that the capital amount standing in the name of Ponnammal the applicant's mother does not belong to the applicant's firm constitute the matter *res judicata* and estop the income-tax authorities from re-opening the same question in the subsequent year?

(3) Is there anything in the language of section 37 of the Act which empowers the Income-tax Officer to require the production of accounts for a period anterior to three years prior to the previous year notwithstanding the restriction in his powers imposed by the proviso to section 22 (4) of the Act?

(4) Is it competent to an Income-tax Officer to draw an inference adverse to an assessee because the latter does not produce accounts which by the proviso to section 22 (4) of the Act the Income-tax Officer is precluded from requiring the production of?"

7. My opinion on the above questions is as below:—

Questions (1) and (2). These two questions may conveniently be answered together. The decision referred to in the questions are filed marked

* Not printed.

Exhibit D.* *Res Judicata* presupposes that there are two opposing parties, that there is a definite issue between them, that there is a tribunal competent to decide the issue and that within its competence the tribunal had done so. In a proceeding before an Income-tax authority none of these various elements which are necessary for the application of the principle of *res judicata* are to be found and in my opinion the doctrine cannot be applied to income-tax proceedings. I am supported in this view by a decision of the Full Bench of the Madras High Court in *Massey & Co., Ltd., v. The Commissioner of Income-tax, Madras*(1), wherein a similar question has been answered in the negative.

I may add that it was the duty of the Income-tax Officer in this case to set at rest his doubts concerning the genuineness of the entries in the books produced, and of the claim made before him that the sums credited in the accounts in the names of ladies represented capital borrowed by them for the purposes of their business. If the evidence on record relating to the previous assessments had been sufficient to clear those doubts he would doubtless have acted on it. This was evidently not the case and in such circumstances I am of opinion that there was nothing to prohibit him from calling upon the petitioners to produce evidence of the facts that they desired to establish.

Questions (3) and (4). These two questions may also be taken up together. The issue of a summons in this case under section 37 was quite unnecessary. The Income-tax Officer himself evidently realised it, for when his summons was not complied with he took no steps to enforce it. Under section 23 (3) however the Income-tax Officer had power to call for evidence on specified points and he made it clear to the petitioners in the notice which he issued to them that he wanted evidence on the question of the ownership of the sums alleged to have been borrowed for the purposes of the business. He went so far no doubt as to specify the kind of evidence that he required, but he also gave the petitioners to understand that he would consider any evidence that they chose to produce on that point. He heard the evidence produced and for the reasons stated by him he declined to place any reliance on it. But the evidence of the old accounts which to the knowledge of the petitioners the Officer regarded as specially important was not produced; and from this the Officer drew the inference that that evidence if produced would have been unfavourable to them. The ground for the decision arrived at in this case was that the petitioners had been given repeated opportunities of proving certain facts the onus of proving which lay upon them and that they had failed to prove them. This decision would stand on this ground even if the petitioners were right in their contention that the Income-tax Officer had no authority to draw any adverse inference from the non-production of the accounts in question. But I am of opinion that their contention is not correct. I am not aware of anything in section 22 (4) or in any other provision of law which could prevent the Officer from forming his own conclusions on matters of fact from the evidence laid before him. He was not bound to believe that evidence if he considered that it was false and that better evidence could have been produced. The right to draw an inference from the non-production of accounts is based on ordinary human conduct and the common course of natural events and has nothing whatever to do with the existence or non-existence of a power to compel their production.

K. S. Krishnaswamy Ayyangar and S. Nataraja Nadar, for the Assesseees in O. P. Nos. 177 and 178 of 1928.

V. V. Srinivasa Ayyangar and P. R. Srinivasan, for the Assesseees, in O.P. Nos. 175, 176, 229 and 253 of 1928.

* Not printed.

(1) 3 L. T. C. 302.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

[O. P. Nos. 177 and 178 of 1928].

The assessees are a Hindu joint family and were sought to be assessed for the year 1926-27 as members of a joint family. They claimed an allowance for interest which they said was paid on sums of money standing in the books as borrowings from the wives of male members. These sums according to the assessees have been standing for several years in their books as moneys which belonged to the ladies and which they lent to the firm and on which interest has been paid to them. So far as the female members are concerned, it is not disputed that they were being taxed separately as if the interest paid to them was income which they derived from moneys which they lent to the firm. This was going on till 1923 when the Income-tax Officer instituted enquiry as to whether these sums were really loans to the trade made by the female members. Notice was given, enquiry was held, affidavits were filed and the Income-tax Officer came to the conclusion that these were loans and the allowance was made for interest which was paid to the female members of the family. This went on according to the petitioners till the accounting year 1925-26. In 1926-27 enquiry was again opened on this question. The Income-tax Officer wanted to re-open the question and he asked the assessees to produce the accounts from 1917-20. A combined notice was issued under sections 22 (4) and 23 (2). The accounts from 1917-20 were not produced, it being alleged that the books were not available as they were lost. Upon that the Income-tax Officer of Sattur disallowed the claim made for reduction on account of interest paid to the female members and his note is "Interest payments to the assessees' female relations have been disallowed as the assessees have withheld the production of earlier books which alone will show whether the amounts standing to their credit are their own Sridhanam amounts or not". He evidently acted on the mere fact of non-production of the account books.

An appeal was made to the Assistant Commissioner of Income-tax who after setting out all the facts in paragraph 2 of his order held that the Income-tax Officer was not precluded from re-opening the question. He made further enquiries, examined the parents and relations of the ladies and came to the conclusion for the reasons given by him that these amounts were not proved to be the Sridhanam moneys of the ladies lent to the firm. He upheld the Income-tax Officer's decision. Then there was an appeal to the Commissioner and he upheld the order of the Assistant Commissioner and refused to refer the questions asked on the ground that no questions of law arose. On a petition to the High Court he was ordered to refer the following questions:—

(a) Whether when in a previous year of assessment a decision was arrived at after investigation and enquiry that certain amounts standing in the name of certain ladies in the petitioners' accounts were the Sridhanam amounts belonging to them and as such the interest paid in respect of the said amounts was held to be a valid deduction, it is open to the Income-tax authorities to reopen the question of the ownership of the amounts in a subsequent year of assessment and whether the authorities are not barred by principles of *res judicata* or otherwise from re-opening the said question.

(b) Whether when amounts are shown in the assessees' account books as the amounts belonging to certain ladies of the family and the Income-tax authorities have treated the said amounts for several years as such and when they have assessed the ladies separately in respect of the said amount on that

basis, it is competent for the authorities to levy assessment in respect of the very same amount on the petitioners, the assessment on the ladies having become final not having been set aside by appropriate proceedings.

(c) Whether in the absence of any affirmative evidence on the part of the Crown it is open to the authorities to presume that the amounts standing *prima facie* in the name of the ladies belonged to the petitioners.

(d) Whether there was any legal evidence before the Income-tax Officer and the Assistant Commissioner in support of their findings as to the ownership of the said amounts.

(e) Whether there is any jurisdiction for the Income-tax authorities purporting to act under section 37 of the Act to call upon an assessee to produce accounts relating to a period prior to three years of assessment and whether any inference can be drawn against the assessee by reason of non-production thereof of such accounts.

(f) Whether when goods are sent to an assessee for the purpose of sale on commission and a certain small amount is charged on the consignor for each bag sent as and for Mahimai which is paid over by the assessee either immediately or subsequently to the trustees of the Mahimai fund intact, the said amount is liable to be assessed for income-tax.

(g) Whether when debts are actually written off by the assesseees as an irrecoverable bad debt it is open to the authorities to disallow a deduction in respect of the same on the ground that the origin of the debt has not been proved.

It is argued before us that where an Income-tax Officer holds an enquiry and comes to a decision, that decision has the force of *res judicata* and precludes the question being re-opened subsequently and that even if not *res-judicata* it operates as an estoppel; secondly that the Income-tax Officer was not entitled to call for accounts relating to a period more than three years prior to the previous year as he is prohibited from doing so by the proviso to section 22 (4), that the requisition for the production of the account books for the years 1917-20 was therefore illegal and consequently no adverse inference can be drawn from the non-production of the account books, nor can the non-production be made the basis of an assessment and that in the present case the Income-tax Officer having proceeded mainly on that ground alone, the assessment levied by him on that footing is illegal.

As regards the question of *res judicata* we do not think the contention can be accepted. The argument for the petitioners is that where an authority is constituted by a statute for determining judicially the legal rights and obligations of parties whether *inter se* or between themselves and the Crown and where that authority has to determine not only whether an obligation exists but also the measure of that obligation, that authority is a Court and the decisions of that authority are final and conclusive subject to such remedies by way of appeal or otherwise as are conferred by law. For this broad proposition there is no authority.

So far as the Income-tax Act is concerned, there is nothing in the Act which states that an Income-tax Officer proceeding to assess the income of an assessee and to determine the amount of such assessment is a Court. On the contrary the provisions of section 37 suggest that except for certain purposes the Income-tax Officer is not a Court.

Section 37 states that the Income-tax Officers specified therein shall for the purposes of Chapter IV have the same powers as are vested in a Court under the Civil Procedure Code when trying a suit in respect of the following matters, namely: (a) enforcing the attendance of any person and examining him on oath or affirmation; (b) compelling the production of accounts and (c) issuing commissions for the examination of witnesses; and that any proceeding before an Income-tax Officer, Assistant Commissioner or Commissioner under this chapter shall be deemed to be a 'judicial proceeding' within the meaning of sections 193 and 228 of the Indian Penal Code. If an Income-tax Officer in making an investigation was a Court, there is no necessity for the provisions of section 37. It is only for the purposes stated in that section that he is to be deemed a Court.

In *Lal Mohan Poddar v. Emperor*(1), it was held that a proceeding before an Income-tax Officer on the production of account books pursuant to a notice under section 23 (2) of the Income-tax Act is a judicial proceeding only for the purposes of sections 193 and 228 but not of section 196 of the Penal Code and that a conviction under section 196 for the production of false accounts is bad in law. The learned Judges (C. C. Ghose and Cammiade, JJ.) observed: "As we read section 37, it seems to us to be clear that the Legislature has for the purpose of punishing offences under sections 193 and 228 of the Penal Code (and under no others) converted proceedings before the officers mentioned therein, which are not judicial proceedings ordinarily, into judicial proceedings".

In *Harmukh Rai Dulichand v. Commissioner of Income-tax, Bengal*(2), the question arose whether an Income-tax Officer is Court. Rankin, C. J. observed: "It has been said that the Income-tax Officer must proceed in a judicial manner and section 37 has been mentioned in this connection. Fundamentally, no doubt, the Income-tax Officer must proceed in a judicial spirit and come to a judicial conclusion upon properly ascertained facts; though I would point out that the Income-tax Officer is not a Court, he has not the procedure of a Court, and he is to some extent a party or Judge in his own case".

In *Mahadev Ganesh v. Secretary of State for India*(3), the question was whether an Officer acting under the Sea Customs Act, 1878, and adjudicating on the question whether a certain property was to be confiscated was a Court and it was held that he was not a Court. Sir Norman Macleod, C. J., observed: "I have no doubt that the Collector, who is not bound to adjudge on confiscation and penalty as if the matter was proceedings in a Court of law according to the provisions of the Civil or Criminal Procedure Code, dealt with the various statements before him in a careful and judicial manner".

The question again arose for decision on a reference in *The Commissioner of Income-tax, Madras v. Messrs. Massey & Co., Ltd., Madras*(4), where the question referred was whether the decision of an Income-tax Officer in a previous enquiry constituted the matter *res judicata* and the Full Bench answered the question in the negative. Though there is no discussion in the judgment of this question as the Judges evidently thought it was not arguable, it cannot be said that because no reasons are given in the Judgment the opinion is not binding on us. It was an answer to a question referred and not merely *obiter*.

(1) 2 I. T. C. 428.

(2) 3 I. T. C. 198.

(3) I. L. R. 46 Bom. 752.

(4) 3 I. T. C. 302.

Reference has been made to *In re Nataraja Ayyar*(1), where the question was as regards the power of the High Court to issue a writ of *certiorari* against an Income-tax Officer who instituted criminal proceedings under section 476 of the Criminal Procedure Code. Sundara Ayyar, J., was of opinion that the High Court had no jurisdiction. Sadasiva Ayyar, J., was of opinion that the High Court had jurisdiction. There are some observations in the judgment of both the learned Judges which it is argued support the contention of the petitioners that the Income-tax Officer is a Court. The facts were that the Income-tax Officer issued a notice under section 476 of the Criminal Procedure Code to show cause why the petitioner should not be prosecuted for making a false statement. Section 37 of the Income-tax Act states that the proceedings under Chapter IV which refer to assessment should be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code. So that where proceedings are sought to be taken for perjury it may well be contended that so far as the proceedings are concerned, the Income-tax Officer should be deemed to be a Court attracting the provisions of the Code as regards revision and appeal to the High Court. So far as we can see, the question was not raised, nor was it necessary to be raised as to whether an Income-tax Officer was a Court when he assessed parties to income-tax. The contention of the petitioner was that the Income-tax Officer in determining the appeal did not act as a Court, that he had no jurisdiction to pass an order under section 476 of the Criminal Procedure Code and that even if he was a Court, he had no jurisdiction to pass the order long after the proceedings terminated. The Public Prosecutor stated that there was no power in the High Court to issue a writ of *certiorari* for various reasons. It was unnecessary for the purpose of that case to decide whether an Income-tax Officer proceeding to assess an assessee was a Court. And if the observations of the learned Judges can be said to lay down any such broad proposition we would respectfully dissent from it.

In this connection we may state that the Income-tax Department has been held in England to be only a department of the Executive and not to be a Court of justice.

In *Local Government Board v. Alridge*(2), Viscount Haldane observed: "My Lords when the duty of deciding an appeal is imposed, those whose duty it is to decide it must act judicially. They must deal with the question referred to them without bias, and they must give to each of the parties the opportunity of adequately presenting the case made. The decision must be come to in the spirit and with the sense of responsibility of a tribunal whose duty it is to mete out justice. But it does not follow that the procedure of every such tribunal must be the same. In the case of a court of law tradition in this country has prescribed certain principles to which in the main the procedure must conform. But what that procedure is to be in detail must depend on the nature of the tribunal * * * *. When, therefore, Parliament entrusts it with judicial duties, Parliament must be taken, in the absence of any declaration to the contrary, to have intended it to follow the procedure which is its own, and is necessary if it is to be capable of doing its work efficiently".

Lord Shaw observed: "The words 'natural justice' occur in arguments and sometimes in judicial pronouncements in such cases. My Lords, when a central administrative board deals with an appeal from a local authority it must do its best to act justly, and to reach just ends by just means. If a statute prescribes the means it must employ them. If it is left without express guidance it

(1) 36 Mad 72.

(2) (1907) 2 Ch. 236.

must still act honestly and by honest means. In regard to these certain ways and methods of judicial procedure may very likely be imitated; and lawyer-like methods may find especial favour from lawyers. But that the judiciary should presume to impose its own methods on administrative or executive officers is a usurpation. And the assumption that the methods of natural justice are *ex necessitate* those of Courts of justice is wholly unfounded. This is expressly applicable to steps of procedure or forms of pleading. In so far as the term 'natural justice' means that a result or process should be just, it is a harmless though it may be a high-sounding expression".

There can be little doubt that Income-tax Officers in conducting enquiries have to act judicially and to exercise their discretion not capriciously but on recognised judicial principles but that would not constitute the Officer making the enquiry a Court.

Reference has been made to *Hill v. Clifford*(1). In this case, the General Medical Council, acting under the powers of the Dentists Act, 1878, made an order directing that the name of one Clifford should be struck off the Register of Dentists on the ground that he had been guilty of professional misconduct. Thereupon his partner gave notice determining the partnership. Suits were filed to determine the validity of the notice and the order of the Medical Council was tendered in evidence. Warrington, J., rejected it and decreed the action of the plaintiff. It was held by Cozens-Hardy, M. R. and Buckley, L. J., that the order was admissible as *prima facie* evidence of the fact that Clifford was guilty of acts infamous or disgraceful in a professional sense. The President Sir Corell Barnes was of opinion that the order was admissible as evidence and conclusive evidence of the fact that the defendant's name had been erased from the register by order of the Council against the defendant for some purposes other than the truth of the fact of misconduct to show the grounds upon which it was made. All that this case decides is that the order of the Medical Council is relevant evidence. It does not support the contention that the Council was a Court.

As regards statutory bodies exercising *quasi* judicial function, the law is thus stated in Halsbury, Laws of England, Vol. XIII, page 362: "The doctrine of estoppel by record has been extended by analogy to the decisions of all tribunals which have jurisdiction, whether by the law of this country, or by the consent of parties, or by the law of the country to whose tribunals the parties have, or may be presumed from their conduct to have, submitted themselves." In paragraph 507 it is observed: "The principle of conclusiveness has been applied to decisions not of record in numerous cases, of which the following are examples: A sentence of expulsion passed by a college; of deprivation by a College Visitor; of trustees dismissing a school-master; an order of the General Medical Council; the award of an arbitrator. So orders of Commissioners of Sewers (not made between the parties litigant) have been held admissible as evidence of reputation, on the express ground that they were adjudications of a Court of competent jurisdiction over the subject matter."

We are of opinion that an Income-tax Officer proceeding to assess an assessee after making an enquiry as contemplated by the Income-tax Act is not a Court and that it cannot be said that the doctrine of *res judicata* applicable to the decisions of Civil Court applies. In this connection we may refer to two cases one cited on behalf of the petitioners and the other on behalf of the respondent.

(1) (1907) 2 C. 236.

Reference has been made by Mr. Krishnaswami Ayyangar for the petitioners to *Hoystead v. Commissioner of Taxation*(1). The question there was whether the beneficiaries were joint owners. The High Court in a previous assessment proceeding had held that six deductions of £5000 should be made on that footing. In the subsequent year the Commissioner allowed only one deduction contending that the beneficiaries were not joint owners within the meaning of the Act. Upon a case stated the Court in Australia upheld the contention that only one deduction of £5000 ought to be made. But their Lordships of the Privy Council reversed the decision on the ground that the previous proceedings estopped the Commissioner from contending that only one and not six deductions should be made. Reliance was placed on the following passage in the judgment of Lord Shaw: "Very numerous authorities were referred to. In the opinion of their Lordships it is settled, first, that the admission of a fact fundamental to the decision arrived at cannot be withdrawn and a fresh litigation started, with a view of obtaining another Judgment upon a different assumption of fact; secondly, the same principle applies not only to an erroneous admission of a fundamental fact, but to an erroneous assumption as to the legal quality of that fact. Parties are not permitted to begin fresh litigations because of new views they may entertain of the law of the case, or new versions which they present as to what should be a proper apprehension by the Court of the legal result either of the construction of the documents or the weight of certain circumstances * * * * *. Thirdly, the same principle—namely, that of setting to rest rights of litigants, applied to the case where a point, fundamental to the decision, taken or assumed by the plaintiff and traversable by the defendant, has not been traversed. In that case also a defendant is bound by the judgment, although it may be true enough that subsequent light or ingenuity might suggest some traverse which had not been taken".

For the Commissioner of Income-tax, reference has been made to *Broken Hill Proprietary Co. v. Broken Hill Municipal Council*(2): the question related to the valuation under the Local Government Act, 1919, of New South Wales. There was an adjudication as to valuation for a previous year and the question arose as to the valuation for the subsequent year. The point of *res-judicata* was raised on the ground that the adjudication by the Court for the previous year would be conclusive as regards the subsequent years. Lord Carson in rejecting this contention stated: "It was also contended before this Board on behalf of the respondents that having regard to the said decision of the High Court of Australia the question raised by this appeal is *res judicata* as between the appellants and the respondents, and the appellants are estopped from contending that such decision of the High Court of Australia is wrong. It has been pointed out that no such question was raised or pleaded either before the District Court or the Supreme Court in New South Wales, nor has there been any adjudication or finding upon it. There is, however, no substance in this contention. The decision of the High Court related to a valuation and a liability to a tax in a previous year, and no doubt as regards that year the decision could not be disputed. The present case relates to a new question—namely, the valuation for a different year and the liability for that year. It is not *eadem questio*, and therefore the principle of *res judicata* cannot apply".

The principle to be deduced from these two cases is that where the question relating to assessment does not vary with the income every year but depends on the nature of the property or any other question on which the rights of the parties to be taxed are based, e.g., whether a certain property is trust property or not, it has nothing to do with the fluctuations in the income; such questions

if decided by a Court on a reference made to it would be *res judicata* in that the same question cannot be subsequently agitated. But if the question is decided by a Court on a reference which depends upon considerations which may vary from year to year, e.g., the case in which the average valuation had to be taken, there could be no question of *res judicata*.

The next question is whether even assuming that the matter is not *res judicata*, it would not create an estoppel by record against the Income-tax Officials.

In this connection the argument of Mr. Krishnaswami Ayyangar is that even treating the Income-tax Officials as a *quasi* judicial body and a Court, the principles of natural justice and expediency ought to prevent Income-tax Officers from going back on their previous decisions. Reference has been made to the passage in Halsbury's Laws of England I have already quoted.

It seems to us that where Income-tax Officials have after enquiry proceeded to assess the assessee on a certain basis, though they may be entitled to re-open the enquiry they cannot arbitrarily change the assessment simply on the ground that the succeeding Officer does not agree with the preceding Officer's finding. The position is just like the position of any two parties who have proceeded on a certain basis in their relations. It may be open to one party to reopen the matter. But if he wants to do so, there should be facts which would entitle him to do it. If fresh facts come to light which on an investigation would entitle the Income-tax Officer to come to a different conclusion from that of his predecessor we think he is entitled to reopen the question. But if there are no fresh facts, it is difficult to see how he can arbitrarily go behind the finding of his predecessor. The same principles of natural justice or judicial dealing which courts impose upon Income-tax Officers would prevent them capriciously setting aside the orders of their predecessors based on enquiry. In the present case if there were no fresh facts, we do not think the Income-tax Officer can simply say that he would not be bound by the order of his predecessor affecting a question like the present, namely, whether a certain sum is the capital of the firm or a loan. But if on investigation any additional facts come to his notice which he considers sufficient, he would be entitled to act upon that additional information and we do not think the Courts of justice can interfere. If there is evidence on which he could have acted it is not for the Court to constitute itself into a Court of appeal and see whether that evidence is sufficient or insufficient.

As regards the question as to the power of the Income-tax Officer to demand the production of accounts beyond three preceding years the provisions of sections 22, 23, and 37 have to be considered. The contention for the petitioners is that in no case can accounts for over three years be called for whatever may be the nature of the enquiry. For the Commissioner of Income-tax it is contended that the limitation as to three years applies to a case where the Officer proceeds to assess under section 23 (4) and that in other cases the Income-tax Officer is not precluded from calling for evidence.

Sections 22 and 23 deal with the return of the income furnished by the assessee for the purpose of being assessed. Sub-section (2) empowers the Income-tax Officer to serve a notice upon the assessee requiring him to furnish within the period specified therein a return in the prescribed form of his total income during the previous year. Sub-section (4) enables the Officer to require the assessee to produce such accounts or documents as the Officer may require.

So far as the accounts are concerned, the proviso says that the Income-tax Officer shall not require the production of any accounts relating to a period more than three years prior to the previous year.

Section 23, sub-section (4) deals with cases where the Income-tax Officer is empowered to make an assessment to the best of his judgment and it says that he can do so if the assessee fails to make his return under sub-section (1) or sub-section (2) of section 22 as the case may be, or fails to comply with all the terms of the notice issued under sub-section (4) of the same section, or having made a return fails to comply with all the terms of the notice issued under sub-section (2) of section 23 which refers to the appearance of the person submitting the return at the office of the Income-tax Officer and the production of any evidence on which such person may rely. Under sub-section (2) of section 23 it is the evidence which the assessee has to rely on that is required to be produced. Section 37 refers to the power to take evidence and empowers the Officer to enforce the attendance of any person, and to examine him on oath or affirmation, to compel the production of documents and to issue commissions for the examination of witnesses.

Reading these sections together we think that the proviso to sub-section (4) of section 22 when read with section 23, sub-section (4) only limits the power to call for accounts for more than three years prior to the previous year when the Income-tax Officer has to make the assessment to the best of his judgment, where the conditions mentioned in sub-section (4) of section 23 exist. Where however during the course of an enquiry the Income-tax Officer is not going to make the assessment to the best of his judgment owing to want of materials but proceeds to make an enquiry as regards the truth or otherwise of the allegations made by the assessee in his return in order to determine whether the assessee has made out his allegations, there is nothing to prevent the Income-tax Officer from requiring the assessee to produce any evidence including accounts. It will be unreasonable to suppose that where, for example, an assessee claims certain deductions and the Income-tax Officer wants to make an enquiry into the truth or otherwise of the allegations it is open to the assessee to refuse to produce any accounts beyond the three years fixed in the proviso to sub-section (4) of section 22, and require the Income-tax Officer to come to a decision on the materials afforded by the three years accounts.

As regards the presumption to be drawn from the non-production of the account books, we think the case will be governed by section 114 of the Evidence Act. Illustrations (g) and (h) refer to cases of non-production of accounts and documents and refusal to answer questions.

Where an assessment is made under section 23 (4) it is difficult to see how an Income-tax Officer can call for the production of books beyond the period specified in the proviso to section 22 and then draw an adverse inference for the purpose of penal assessment. It will really be defeating the protection given by section 22 (4). But where the accounts are called for otherwise than for that purpose there is no reason why the presumption should not be drawn as in any ordinary case.

In this case the accounts were called for during the course of the enquiry as to whether the deduction claimed by the assessee should be granted or not, and we think that the Income-tax Officer was entitled to draw an adverse inference owing to the non-production of the account books. It is a question of fact whether the books were available or not. The assessee says they were lost or des-

troyed but the Income-tax Officer does not believe it. It is not for us to say whether the Income-tax Officer was justified or not in his conclusion.

This disposes of all the points argued before us. The petitioners will pay the Respondent Rs. 250 for costs.

JUDGMENT.

[O. P. Nos. 176 and 229 of 1928].

These petitions are governed by our decision in O. P. Nos. 177 and 178 of 1928 as only the points argued in O. P. Nos. 177 and 178 of 1928 have been pressed before us in these two petitions.

The petitioners will pay the Respondent Rs. 250 for costs.

JUDGMENT.

[O. P. Nos. 175 and 253 of 1928].

In these two petitions the same two questions namely, the question of *res judicata* and the inference to be drawn from the non-production of account books were argued, and for the reasons given in O. P. Nos. 177 and 178 of 1928 the same answer will be given in these two petitions as was given in O. P. Nos. 177 and 178. The petitioners will pay the Respondent Rs. 250 for costs.

[340] PRIVY COUNCIL.

ON APPEAL FROM THE HIGH COURT OF JUDICATURE AT BOMBAY.

PRESENT:

Lord Buckmaster, Viscount Dunedin, Lord Tomlin, Sir George Lowndes and Sir Binod Mitter.

(4th November, 1929).

The Commissioner of Income-tax, Bombay .. Appellant.*

v.

The Ahmedabad New Cotton Mills Co., Ltd. .. Respondents.

Indian Income-tax Act (XI of 1922), Secs. 3 and 13—Undervaluation of opening and closing stock of a year—Income-tax Officer revaluing closing stock only at true value—Refusal of assessee's claim for revaluation of opening stock—Opening and closing stock to be given true value.

The assessees in their return of income put in a profit and loss account and a balance sheet wherein their opening and closing stock for the year were written down at an undervaluation. The Income-tax Officer revaluing the closing stock only at its true value made an assessment, declining to revalue the opening stock at its true value as claimed by the assessees.

HELD, that the real profits of the assessees could not be ascertained by merely raising the valuation of the closing stock, not taking into consideration the similar undervaluation of the opening stock.

* (1930) 57 I. A. 21; 54 Bom. 213; 58 M.L.J. 204; 33 B. L. R. 358; 31 C. M. N. 262; 51 L. L. J. 128; A. I. R. (1930) P. C. 56.

Judgment of the High Court affirmed.

Appeal (Privy Council Appeal No. 43 of 1929), preferred against the Judgment of the High Court at Bombay, (Marten, C.J., and Kemp, J.), reported in 3 I. T. C. 91.

A. M. Dunne, K. C. and Reginald Hills, for Appellant.

A. M. Latter, K. C. and C. J. Colombos, for Respondent.

JUDGMENT.

LORD BUCKMASTER: The question submitted for the opinion of the High Court is in the following term: "When the opening and closing stocks" their Lordships think that there ought to be introduced "of a business" "are both undervalued, whether the real profits of the company of a particular year can be ascertained by merely raising the valuation of the closing stock, not taking into consideration the similar undervaluation of the opening stock"; and the answer is that in the opinion of the Board, they cannot.

The method of introducing stock into each side of a profit and loss account for the purpose of determining the annual profits is a method well understood in commercial circles and does not necessarily depend upon exact trade valuations being given to each article of stock that is so introduced. The one thing that is essential is that there should be a definite method of valuation adopted which should be carried through from year to year, so that in case of any deviation from strict market values in the entry of the stock at the close of one year it will be rectified by the accounts in the next year. It may of course, be that in so adjusting the figures of stock there may be special cases in which the valuation is so treated as justly to cause it to be open to dispute. But their Lordships have nothing whatever to do with that in this particular case. They are asked to answer a perfectly simple question which, upon the face of it, in the opinion of the Board, would answer itself. If the method of altering both valuations is not adopted it is perfectly plain that the profit which is brought forward is not the real one. It may be more or it may be less, but it has no relation to the true profit if the stock is valued on one basis when it goes out without considering the value of the stock when it comes in. When, therefore, there is undervaluation at one end, the effect is to cause both a smaller debit in respect of the stock introduced into the next account and a larger sum for profits realised by the sale, change in market values being immediately reflected in the price obtained for the goods that are sold; in these circumstances to contend that there should be undervaluation at one end and not at the other is to raise an argument which their Lordships cannot accept.

Further, section 13 of the Indian Income-tax Act, 1922, says: "Income profits and gains shall be computed for the purposes of sections 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee". Of course, that must be the method regularly and properly employed by the assessee, and it has never been suggested here that this has not been the method regularly employed, nor, in their Lordships' opinion, was it improper.

Their Lordships have merely to consider the point raised by the Commissioner, and it is sufficient to say that for the above reasons the judgment of the High Court is, in their opinion, right.

Their Lordships will therefore humbly advise His Majesty that the appeal be dismissed with costs.

Solicitor, India Office, Solicitors for Appellant.

Barrow, Rogers and Nevill, Solicitors for Respondents.

[341] IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Niamatullah

(21st November, 1929).

Ram Prasad, Principal Agent of Tehri State . . . Assessee.

v.

The Commissioner of Income-tax, United Provinces . . Referring Officer.

Indian Income-tax Act (XI of 1922), and Government Trading Taxation Act (III of 1926)—Applicability of the Acts to Tehri State—Government Trading Taxation Act, if ultra vires of Indian Legislature—Sale of State timber in British India—Assessment on estimated profits from timber sale—Trading in British India.

The Government Trading Taxation Act, III of 1926 is not ultra vires of the powers of the Indian Legislature, and this Act, and the Indian Income-tax Act, XI of 1922, are applicable to the Tehri State which is part of His Majesty's Dominions, being a territory under His Majesty's protection.

The assessee, the Tehri State, sold timber grown in the State by acceptance at the State capital of the offers received at the annual auction held at Dehra Dun in British India, the monies due to the State thereunder being deposited by the purchasers in the Dehra Dun branch of the Imperial Bank of India. The State had also a trading department in charge of a State official with head-quarters at Hardwar which arranged for sales in British India.

On an assessment for the year 1926-1927 in respect of profits arising from the timber business in 1925-1926, worked out at 35 per cent. of the gross receipts, the State contended inter alia that the Government Trading Taxation Act of 1926, did not apply in respect of transactions prior to the 1st of April 1926, that the sale proceeds were capital receipts and that there was no trading in British India.

HELD, that the acts of the State constituted "trading in British India" and in view of Sec. 3 of the Government Trading Taxation Act, tax for the year 1926-1927 was to be paid on the profits earned in the year 1925-1926, and

(2) that the assessed amount represented not capital but estimated profits from the business of growing and felling timber.

Case [Miscellaneous Case No. 671 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

This case was originally referred for the decision of the High Court at the request of the assessee while the case was still pending before me in appeal. The reference was thus premature and was accordingly returned by the order of the High Court, dated March 4, 1929, with the direction that it should be re-stated after the final order has been passed. Now that the assessment has been finally disposed off, the case is stated for the decision of the High Court, under section 66 (2) of the Indian Income-tax Act.

2. The Tehri State was assessed by the Assistant Commissioner of Income-tax on February 11, 1928 in respect of its income arising from business carried on in the year 1925-26, under the Government Trading Taxation Act read with the Indian Income-tax Act.

3. The State carried on its business in the following two ways:—

(i) It sold its trees to contractors, holding a preliminary auction at Dehra Dun and the final auction at the State Capital, while the money due to the State was deposited in a number of cases in the Imperial Bank of India, Dehra Dun. As these receipts obviously included the profits arising to the State from these payments made by contractors, in the Imperial Bank of India, such profits were included in the assessment.

NOTE.—The sentence in the appellate order reading: "The State sold its trees to contractors who are resident in British India holding a preliminary auction at the State capital . . . is manifestly an error by elision. It was clearly intended to read: "holding a preliminary auction in Dehra Dun followed by a final auction at the State capital," because it is no one's case that the preliminary auction was at the State capital. This is clearly a stenographic error.

(ii). The State had also a trading department which has now ceased to exist and to which trees were sold as if it were an ordinary contractor. The department, after cutting down the timber, floated it down across the great river to Hardwar in the United Provinces and Abdullahpur in the Punjab. This department known as the "Departmental Timber Operations" with its headquarters at Hardwar, came into existence at a time when the State found itself in a difficulty in selling the forest produce to contractors as the latter had formed themselves into a ring. The State, therefore, availed itself of the assistance of one of its biggest contractors—Rai Bahadur Pandit Ghananand—who offered to effect the sale of forest produce in a particular manner in order to break the ring. He ran the business for some time and then fell ill and died. As he was seriously ill, he made a request to the State that some one else should be deputed to take charge of the work from him. It is not clear from informations furnished by the State at what precise date Rai Bahadur Pandit Ghananand died and his connection with the business terminated. As his brother refused to carry on the contract or be responsible for anything as from the date of the original contractor's death, the State appointed one Pandit Sadanand Naithani, one of its own officials, in order to carry on the work on the same conditions on which the original contractor had been appointed. It was urged that the business carried on by the Departmental Timber Operations has nothing to do with the State and that the income arising therefrom should not be included in the assessment of the State. The State, however, adduced no evidence to prove this and the assessing officer held that all the operations carried on by this department were those of the State.

4. The assessment was accordingly made on the profits of the Departmental Timber Operations as also on the profits contained in the sums credited by the contractors to the State account in the Imperial Bank at Dehra Dun.

5. It would perhaps be useful to mention how the profits were arrived at. The State had worked out an income of Rs. 867 as the profit of the Departmental Timber Operations in the following manner:—

Gross receipts	...	...	...	Rs. 8,70,800
Deduct—				
(a) Working and establishment expenses and other charges	...	...	Rs. 3,50,413	8,69,933
(b) Royalty paid to the State forest department	...	...	4,73,490	
				<u>867</u>

The State showed this very small profit of Rs. 867 because a very large sum was debited to the account as royalty as if it was an expenditure incurred in earning the profits. The profits, on adding the amount debited as royalty, came to Rs. 4,74,357. The contention of the State is that the royalty represents the price of the raw forest produce, i.e., the cost of growing the forest to the State and as such is not assessable. The manner in which it is calculated is described to be in the following manner. The cost of cutting and transporting the timber to the place of sale is calculated and an amount varying from 10 per cent. on the expenditure is allowed to the contractor as profit. The balance of the value of the tree is taken by the State as royalty. For instance, if a tree were sold for Rs. 100, and it cost Rs. 50 to cut and transport it, the profit allowed to the contractor would be some sum between Rs. 5 and Rs. 10 and the balance, i.e., Rs. 40 to Rs. 45, would be royalty. The State, however, adduced no evidence to support this contention. It was further represented that the business carried on by the Departmental Timber Operations had actually resulted in a loss to the State and that the expenditure incurred by the State in producing its trees, whatever it may be, was also to be set off against the receipt. The State, however, did not adduce any evidence to show what this expenditure was. It was, therefore, difficult to find out a sound basis for calculation. And for this purpose the financial accounts of the Forest Department of the United Provinces, which have been published in the annual reports, were examined for several years and it was found that they yielded a profit of 44 per cent. after allowing all expenditure "direct" and "indirect" from the gross receipts. The "direct expenditure" includes mainly the cost of marking trees, checking export and generally expenditure incidental to the realization of the revenue of the year as also the cost actually incurred in converting forest produce into marketable timber and exporting it to market, while "indirect expenditure" is that incurred on tending woods, building and repairing roads and houses and generally improving and maintaining the estate. The rate of profit disclosed by the figures contained in the annual reports of the Forest Department was considered to be a reasonable guide in estimating the profit of the Tehri State forests and, in view of the representations made by the State, a wide margin was allowed and a rate of 40 per cent. was applied to the amount of Rs. 4,74,357, i.e., the gross receipts minus working and establishment and other charges. The assessment was accordingly made on an income of Rs. 1,89,742.

As regards the profits on the payments made by the contractors in the Imperial Bank of India, Dehra Dun, the State supplied the assessing officer with the information that Rs. 5,06,652 had been received in the Imperial Bank of India and the assessing officer estimated the profit to be Rs. 2,02,660 at a

rate of 40 per cent. of these receipts. It was, however, represented in appeal that the figures furnished by the State at the time of the original assessment were not correct and that the actual receipt amounted to only Rs. 3,74,464 and not Rs. 5,06,652. The Commissioner accepted the revised figures and took the profits to be Rs. 1,49,785 instead of Rs. 2,02,660. The total income was accordingly reduced from Rs. 3,92,402 to Rs. 3,39,527 and the income-tax and super-tax demand was reduced to the following figures:—

		Rs.	a.	p.		Rs.	a.	p.
Income-tax	...	31,830	11	0	as against	36,787	11	0
Super-tax	...	18,095	7	0	as against	21,400	2	0

The rate of profit applied was, however, challenged in appeal and the Commissioner of Income-tax decided to give the State a further opportunity to prove that the rate of profit in the State was less than 40 per cent. and, therefore, remanded the case to the Assistant Commissioner of Income-tax for further detailed enquiries and for the examination of such evidence as might be produced before him on behalf of the State. The Assistant Commissioner made a detailed enquiry and gathered some valuable information from the records of the Forest Department which are embodied in his report, dated September 13, 1928 (appendix E).^{*} He came to the conclusion that the rate applied by him was quite fair and that there was no reason for him to vary the original estimate. In order, however, to be on the safe side, I made a further reduction in appeal (appendix F)^{*} and applied a rate of 35 per cent. as against 40 per cent. applied by the Assistant Commissioner of Income-tax and took the profits to be Rs. 2,97,087 and reduced the original demand to:—

	Rs.	a.	p.
Income-tax	..	27,851	15 0
Super-tax	..	18,567	15 0

6. The State has not accepted the assessment and has demanded a reference to the High Court on nine grounds (appendix B)^{*}. The points of law which arise from them are stated as follows:—

- (i) Whether the Government Trading Taxation Act and the Indian Income-tax Act are applicable to the Tehri State?

In the opinion of the Commissioner the answer is in the affirmative. It may, however, be observed that it was conceded in the course of the appeal before my predecessor (vide his appellate order dated March 14, 1928—appendix A)^{*} that the State “had no wish to challenge the jurisdiction of the Income-tax Department. It was rather a question of comity, i.e., a political question.” In this connection my predecessor rightly observed that it was his duty to apply “the provisions of the law without any reference to political considerations.”

- (ii) Whether since the Government Trading Taxation Act only came into force on April 1, 1926, there is any liability for assessment with reference to transactions which took place before that date?

My predecessor has discussed this point in detail in paragraph 3 of his appellate order, dated March 14, 1928 (appendix A)^{*} and has justly remarked that: “The fact that the Government Trading Taxation Act only came into force on April 1, 1926 does not mean that the profits of the preceding year shall not form the basis of

the assessment to income-tax in the year 1926-27''. The Commissioner is of opinion that the question should be answered in the affirmative.

- (iii) Whether the royalty is nothing but the price of the forest produce as it stands in the ground and, therefore, not assessable?

There is nothing on the record to show that the amount of royalty debited to the accounts does actually represent the price of the forest produce to the State. In effect it is nothing but a portion of the gross profits which is taken by the State on its transactions. I, therefore, do not think the question can be answered in the affirmative.

- (iv) Whether the acts of the State in arranging for the sale of timber and in receiving the proceeds of the contracts in British India constitute trading in British India?

This appears to be more a question of fact than of law, but as the matter is not free from doubt, it is also being stated. The question has been discussed in detail in paragraph 6 of my predecessor's appellate order, dated March 14, 1928 (appendix A)*. I do not think it necessary to add anything to what has been said there and, for the reasons given therein, I am of opinion that the answer to this question is in the affirmative.

7. Certain other grounds given in appendix B* have been taken by the assessee but they were either never raised in appeal and as such do not arise out of the order passed under section 31 of the Act or raise a mere question of fact or are mere amplifications of the grounds already dealt with and have not, therefore, been stated.

8. The relevant portion of the revised statement of the case was sent to the assessee for representation and observations, if any, and a copy of his representation, dated April 28, 1929 as well as copies of the Home Member's letter No. C. 1089, dated August 27, 1928, and of the petition dated January 1, 1929, referred to in paragraph 5 thereof, are appended as appendices G,* H* and I* for the information of the Hon'ble High Court. I do not consider it necessary to make any alteration or addition.

9. I may further submit that appendices F,* G,* H* and I* have only been attached to this statement as all other appendices quoted therein are contained in the previous statement of the case already submitted.

Sir Tej Bahadur Sapru, for the Assessee.

The Government Advocate, for the Crown.

JUDGMENT.

This is a reference by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act of 1922.

The assessee is the Tehri State. It appears that the State has grown timber within its territory and annually it arranges to sell the timber at two places in British India, namely, Hardwar in the United Provinces and Abdullapur in the Punjab. The method of business is this. Annual auctions are held in Dehra Dun and certain prices are offered. These offers are communicated to the State capital, and there, on their acceptance, money is deposited by the pur-

chasers in the Imperial Bank of India, in its Dehra Dun Branch. It also appears that, later on, the State appointed a certain gentleman, by the name of Pandit Ghananand, to carry on the sale of timber. He having died shortly after a State official was appointed to carry on the business. This was Pandit Sadanand.

The year on the basis of the income of which income-tax is to be calculated is 1925-26. The tax is to be paid in the year 1926-27. An assessment having been proposed, the State opposed it on several grounds. There was an appeal to the Commissioner of Income-tax and he considerably reduced the proposed tax. Being, however dissatisfied with the ultimate assessment, the Tehri State asked for a reference, and four points have been put before us for our opinion. These are: (1) Whether the Government Trading Taxation Act and the Indian Income-tax Act are applicable to the Tehri State? (2) Whether since the Government Trading Taxation Act only came into force on April 1, 1926, there is any liability for assessment with reference to transactions which took place before that date? (3) Whether the royalty is nothing but the price of the forest produce as it stands in the ground and, therefore, not assessable? (4) Whether the acts of the State in arranging for the sale of timber and in receiving the proceeds of the contracts in British India constitute trading in British India?

The case for the assessee has been very ably and at some length argued by Sir Tej Bahadur Sapru, and we are greatly indebted to him for his illuminative arguments.

The first point is that the Tehri State is not amenable to the jurisdiction of the Indian Legislature, and neither the Income-tax Act nor the Government Trading Taxation Act can apply to the State. To start with, we have to see whether the Government Trading Taxation Act (III of 1926), is applicable; for that Act has, to some extent, amended and explained certain provisions of the Indian Income-tax Act of 1922. By the preamble of the Government Trading Taxation Act we are told that this Act was meant "to determine the liability of certain Governments to taxation in British India in respect of trading operations." The object, therefore, of the Act is to tax Government who may be trading in British India. The Legislature deliberately has set out on taxing Governments. Section 2 of the Act reads as follows: (1) Where a trade or business of any kind is carried on by or on behalf of the Government of any part of His Majesty's Dominions, exclusive of British India, that Government shall, in respect of the trade or business and of all operations connected therewith, all property occupied in British India and all goods owned in British India for the purposes thereof, and all income arising in connection therewith, be liable (a) to taxation under the Indian Income-tax Act, 1922,....." By sub-section (3) of the same section 2, we are furnished with the meaning of the expression "His Majesty's Dominions." The expression is defined to include "any territory which is under His Majesty's protection.....", Now, the question is whether the Tehri State is part of His Majesty's Dominions. If it is, the Government Trading Taxation Act of 1926 would be applicable, by virtue of sub-section 1 of section 2. The treaty between the Tehri State and the British Government has been read out to us. It will be found at page 34 of Vol. I of Treaties, Engagements and Sanads by Aitchison. The Sanad granted to the Rajah of Garhwal concludes with the following sentence:—"While these conditions shall be faithfully observed, the British Government will guarantee the Rajah and his posterity in the secure possession of the country now conferred upon him and will defend him against his enemies." The sentence quoted above in our opinion, furnishes to us an answer as to what is meant by

the phrase "His Majesty's protection", to be found in section 2 (3) of the Government Trading Taxation Act. In our opinion the Tehri State is included in a territory which is under His Majesty's protection. It would follow, as we have already mentioned, that the Government Trading Taxation Act of 1926 is applicable to the Tehri State.

Now, let us see what is the significance of the passing of the Act III of 1926. By sub-section 2 of section 2, "For the purposes of the levy and collection of income-tax under the Indian Income-tax Act, 1922..... any Government to which that sub-section applies shall be deemed to be a 'company' within the meaning of that Act, and the provisions of that Act shall apply accordingly." The result is that within the meaning of section 3 of the Indian Income-tax Act of 1922, a Government, which carries on trade in British India, is to be treated as a company. The trading 'company' is liable to pay income-tax under section 3 of the Act of 1922. The relevant portion of that section is as follows:—"Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year....., tax shall be charged..... in respect of all income, profits and gainsof every individual, Hindu undivided family, company, firm and other association of individuals." The trading Government as a 'company' becomes liable to pay income-tax under section 3.

The learned counsel for the assessee has argued that under Sec. 65 of the Government of India Act, the Indian Legislature has power to make laws only for persons within British India and the Tehri State being not a person within British India is not subject to the Indian Legislature. In this view, the learned counsel went on to argue, the whole Act III of 1926 was *ultra vires* of the Indian Legislature. We do not think that this argument is quite sound. The English Interpretation Act of 1889, by Sec. 19, defines the word "person". Sec. 19 runs as follows:—"In this Act, and in every Act passed after the commencement of this Act, the expression 'person' shall, unless contrary intention appears, include any body of persons, corporate or incorporate." It may be that the person who governs the State is a single individual or a body of persons. In either case, the Government authority, single or several in number, will come within the definition of the "person" in section 65 of the Government of India Act, and those persons, carrying on business within British India would be subject to any law that the Indian Legislature should frame and promulgate. The object of the Income-tax Act is to charge income acquired in British India, and it is not in the contemplation of the Act to claim anything in respect of something done in the territory of a Government which may have sovereign rights within its own territories. In our opinion the Act III of 1926 was *intra vires* of the Indian Legislature.

Now we come to question No. 2. The argument is, that the income that is being taken into consideration, for taxation accrued to the State in 1925-26, that the Government Trading Taxation Act came into force on the 1st April 1926 and that, therefore, it could have no application to the income which was earned in the previous year (1925-26). On the face of it, this argument is very attractive, but in view of the language employed in section 3 of the Indian Taxation Act, we do not think that it has much force. The Tehri State, we have been told, has continued this business in years subsequent to 1925-26, and the Income-tax Department has sought to assess it for the year 1926-27. The tax is to be paid in and for that year. The Income-tax Department is armed with powers to tax the Tehri State any time after the 1st April 1926. That being so, let us read section 3 of the Act III of 1926. We have already read it once before. Now substituting the years with which we have to deal the section would read as follows:—"Where any Act of the Indian Legislature enacts that

income-tax shall be charged for the year 1926-27..... tax..... shall be charged for the year 1926-27..... in respect of all the income, profits and gains of the previous year (1925-26)....." This is the natural reading of section 3 in view of the facts before us. It seems to be quite clear to us that the tax which has to be paid by the Tehri State for the year 1926-27 is to be paid on the amount of profits earned by it in the year 1925-26. If the State decided to stop its business, say, in the year 1930-31, the tax paid by it, in 1930-31, on the basis of the income of 1929-30, would be liable to be refunded, in so far as the income of the year 1930-31 fell short of the income earned in 1929-30.

Now we come to the third point. The argument of the learned counsel for the assessee is that the money received is really the value of the capital, which has changed its shape, and there are no profits. This really, in our view at any rate, is a question of fact. How the Income-tax Department has looked upon the matter is this. By sale of timber the State is supposed to have made profits. For growing timber a certain amount of capital expenditure is necessary. The British Indian Government has also extensive forests. It employs officers, spends money, sells timber and makes a profit. The Income-tax Department assumed, in the absence of any evidence to the contrary, that the Tehri State does the same. The net profits made by the British Indian Government amounts to about 44 per cent. The Commissioner of Income-tax reduced the profits which the Tehri State, presumably, made to 35 per cent. Now, to go back to the argument of royalty, as we have already stated, it is virtually a question of fact. The question is whether what has been received by the Tehri State is the value of its capital, or whether it includes capital and profits. We have already mentioned that the State carries on this business of growing timber and selling it. This presumably, is done for profit. We have already stated that the British Indian Government does the same thing and makes a profit. It is, therefore, reasonable to expect that all the money that was sunk in the business brought back not only itself but something more, in the shape of profit. If it were the case that what were the receipts were only the capital, which had changed its shape, the argument of the learned counsel would have been very good. We find that the amount on which the tax has been assessed, represents no capital but only the estimated profit. In this view, the answer that we should return is that only the income has been taxed and not the capital.

Coming to the fourth point here again is a question of fact, although the learned Commissioner was doubtful whether it was purely a question of fact or partly a question of law. The question is whether the acts of the State in arranging for the sale of timber and in receiving the proceeds of the contracts in British India constitute "trading in British India". We are of opinion that the answer must be in the affirmative. The sales were arranged in British India and the money was received in British India. What remained to be done in the capital of the State itself was the acceptance of the offer made by the purchaser. We do not think that the matter requires much discussion. The money was received by the Imperial Bank at Dehra Dun as the agent of the Tehri State. The receipt by the Bank was a receipt on behalf of the State. As already stated, we answer the question in the affirmative.

The result is that none of the grounds taken by the Tehri State appears to be tenable.

Let a copy of this Judgment be sent to the Commissioner of Income-tax as the answer to his reference to this Court.

The learned Government Advocate is entitled to a fee of Rs. 250, if he files a certificate of fee within a month.

(342) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

Before Mr. Macnair and Mr. Munje, Additional Judicial Commissioners.

(22nd November, 1929).

Ballarpur Collieries

.. Assessee.*

v.

The Commissioner of Income-tax, Central Provinces .. Referring Officer.
and Berar*Indian Income-tax Act (XI of 1922), Secs. 10 (2) (vi) and 24—Loss in business—Depreciation allowance, if claimable—Scope of proviso—Business loss, if to be increased by depreciation allowance.*

The assessee, a registered firm owning collieries, returned a loss of over six lakhs for the year 1928-1929, including therein an amount of over 2 lakhs on account of depreciation of buildings, machinery, etc., used for the purpose of the business and claimed to set off this loss against the other income of the members of the firm under Sec. 24 of the Income-tax Act. The Income-tax Officer refused to make any allowance for depreciation on the ground that as the firm had suffered a loss, depreciation could not be allowed for that year but must be carried forward under section 10 (2) (vi) proviso (b).

HELD, that the assessee was entitled to the depreciation allowance under section 10 (2) (vi) and to increase the business loss thereby.

Case [Miscellaneous Judicial Case No. 32 of 1929], stated under 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Central Provinces and Berar, for the opinion of the High Court.

CASE.

Rai Bahadur Bansilal Abirchand of Kamptee and the Hon'ble Sir Maneckji Dadabhoy, K.C.I.E., Kt., of Nagpur, form 4 different partnerships for 4 different collieries, i.e., Ghughus Colliery, Pisgaon-Rajur Colliery, Sasti Colliery, and Ballarpur Colliery. Each of the partners has an eight annas share in the partnership. These four partnerships have, for the purposes of Income-tax, been registered on the 3rd January 1929 by the Income-tax Officer of Wardha within whose jurisdiction Ballarpur, the head-quarters of the firm, is. Since all the four partnerships are between the same persons, the designation of the firm is put down in the return under section 22 (2) as "Ballarpur Colliery". The return of income for the year 1928-29 showed that the firm in its previous year had suffered a loss of Rs. 6,35,011. This sum included the following amounts on account of depreciation on plant, machinery and buildings, etc., of the collieries:—

	Rs.
Ballarpur	.. 32,523
Ghughus R. I.	.. 27,612
Ghughus, Pits 2 and 3	.. 40,372
Pisgaon	.. 89,009
Sasti	.. 37,111
	<hr/> 2,26,627

The Income-tax Officer, Wardha, after disallowing certain items claimed as expenses held that the net *business loss* was Rs. 2,94,772. In framing his calculations he made no allowance for depreciation on the ground that "All the collieries show loss and hence depreciation cannot be allowed this year. They will be carried forward for being allowed in future."

2. Against this order of the Income-tax Officer an appeal was filed before the Assistant Commissioner, Nagpur, in which objections were taken to the disallowance of certain items and in which it was contended that the depreciation allowance claimed should not have been carried forward for the purpose of being allowed in future years, but should have been allowed to be added to the loss of the year so that the total loss could be set off against the *personal incomes* of the two different partners in this firm. The latter claim was rejected by the Assistant Commissioner who observed: "As there has been no profit, no depreciation could be allowed, vide Ruling of the High Court of Lahore in the matter of the *Income-tax Commissioner v. Messrs. M. D. Radhakisan & Sons of Rawalpindi*(1)". In parenthesis the Commissioner would remark that the quotation of this ruling is inappropriate as neither of the points dealt with there are relevant to the present case.

3. The firm has now requested, under section 66 (2) of the Indian Income-tax Act, that the following questions of law be referred for the decision of the High Court:—

- (a) Whether the depreciation allowance under section 10 (2) (vi) of the Income-tax Act is claimable by an assessee only if the use or working of the machinery, plant, etc., depreciating brings profits or gains to the assessee and does not result in loss in the year for which the allowance is claimed?
- (b) Whether the proviso (b) to section 10 (2) (vi) is a bar to the claim of depreciation allowance where the assessee owning the machinery, plant, etc., has income, profits or gains chargeable under the Act and assessed to income-tax for the year in respect of which the depreciation allowance is claimed?
- (c) Whether on the facts of this case the disallowance of the depreciation allowance by the Income-tax authorities was legal or authorised under any of the provisions of the Act?

A copy of the application is attached (App. A.)*

4. In the opinion of the Commissioner, the second question does not arise. The assessee in this particular instance is a firm which has no other income, profits or gains than that received from the collieries. It is admitted that each partner in the firm has other income against which his loss for the partnership can be set off, and the point in issue is the amount of that loss, that is to say, it will depend on the decision of the first question of law stated. Similarly, the Commissioner considers that the third question framed by the assessee is merely another form of the first. He is thus unable to state those questions for the consideration of the Court.

5. The first question can, in the opinion of the Commissioner, be more precisely stated, and is therefore stated as follows:—In view of the provisions of section 10 (2) (vi) of the Indian Income-tax Act, 1922, can an assessee claim in

* Not Printed.

(1) 3 I. T. C 73.

the case of a business which has resulted in a loss, that the amount of that loss shall be increased by adding the amount of depreciation calculated in the prescribed manner?

6. The Commissioner is of opinion that a loss resulting from a business in a given accounting period cannot be increased by adding an allowance for depreciation. The latter is not an actual loss but reflects a decrease in the assets of the business which the Income-tax Act allows to be set off against any profits which arise. The answer to the question propounded is therefore, in the negative.

P. R. Srinivasan, Advocate and *A. D. Mande*, Pleader for the Assesseees.

D. N. Chowdhri, for the Crown.

JUDGMENT.

Rai Bahadur Bansilal Abirchand and Sir Maneckji Dadabhoy are partners in a firm designated the Ballarpur Colliery. The return of income for the year 1928-29 shows that the firm had suffered a loss of over six lakhs including an amount of over two lakhs on account of depreciation of buildings, machinery etc., used for the purposes of the business of the firm. The income-tax authorities in calculating the net business loss of the firm made no allowance for depreciation stating that as the firm had suffered a loss depreciation could not be allowed for the calculation of that year, but would be carried forward for being allowed in future. The firm desires that the allowance for depreciation should be taken into consideration for the purpose of calculating the loss for the year in question. The members of the firm have other income against which the loss of the firm, as it is registered, can be set off under the provisions of section 24 of the Indian Income-tax Act and therefore desire that the net business loss of the firm should be held to be as large as possible.

2. The question which arises has been thus stated by the Income-tax Commissioner:—"In view of the provisions of section 10 (2) (vi) of the Indian Income-tax Act, 1922, can an assessee claim, in the case of a business which has resulted in a loss, that the amount of that loss shall be increased by adding the amount of depreciation calculated in the prescribed manner?"

The question does not refer to the fact that the assessee is a registered firm and it has been argued before us that a registered firm cannot be described as an assessee. Section 24 (2) of the Act shows that a registered firm can be an assessee. The fact that the assessee is a registered firm will be taken into consideration in my discussion of the question. I note that the word "loss" in the question means a loss of profits or gains which makes the provisions of section 24 applicable.

3. In order to understand the provisions of section 10 of the Indian Income-tax Act it is necessary to refer to some of the preceding sections. Section 6 states that different heads of income, profits and gains shall be chargeable to income-tax. Each of the succeeding sections gives instructions regarding the manner in which one head of income, profits and gains is chargeable. Section 10 refers to the tax payable by an assessee under the head "business". It does not take into consideration profits or gains under any other head. It does not refer to the rate of tax which is elsewhere stated to be governed by the total income of the assessee.

4. Now section 10 (2) states that the profits or gains of any business carried on by an assessee shall be computed after making certain allowances. It gives no definite instructions for computing the loss of any business and it cannot be assumed that loss is calculated in exactly the same way as profits or gains. Clause (vi) (b) of the sub-section enunciates a special proviso regarding the allowance for depreciation:—"Provided that where full effect cannot be given to any such allowance in any year owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or if there is no such allowance for that year, be deemed to be the allowance for that year, and so on for succeeding years." In *Karam Ilahi Muhammad Shafi v. Chief Commissioner, Income-tax, Delhi*(1), it was considered that the profits or gains referred to were profits or gains generally from whatsoever source derived. With the greatest respect I must dissent from this opinion; section 10, as I have remarked, deals solely with the profits or gains of any business carried on by the assessee. I remark that it would be still more difficult to hold that the profits or gains included profits or gains of a member of the firm which carried on the business. In my opinion, however, the provisions of section 10 (2) (vi) (b) give no assistance in the decision of the question referred to the Bench. In the first place, section 10 refers to the computation of profits and does not deal with computation of loss. In the next place, the proviso which I am considering deals with the case where effect cannot be given to an allowance owing to there being no profit; even if there is no profit in the business I consider that effect can be given to the allowance, if the assessee (or where the assessee is a firm, all the individuals who constitute the firm) can benefit by that allowance by virtue of the provisions of section 24.

5. The question with which I have to deal relates to the calculation of "loss of profit or gains" for the purpose of interpreting the provisions of section 24 of the Indian Income-tax Act. This section is as follows:—

- (1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year.
- (2) Where the assessee is a registered firm, and the loss sustained cannot wholly be set off under sub-section (1), any member of such firm shall be entitled to have set off against any income, profits or gains of the year in which the loss was sustained in respect of which the tax is payable by him such amount of the loss not already set off as is proportionate to his share in the firm.

It is clear that the loss to which sub-section (2) refers is "loss of profits or gains". This phrase is unusual, but must, when the loss is under the head "business", mean loss on the year's working. When the general principles on which profits or gains of a business are computed are utilised to ascertain the result of the year's working and the calculation shows that there has been a loss, that is a loss of profits or gains. Now, clause (vi) (b) of section 10 (2) does not enunciate a general proposition regarding the calculation of the result of a year's business. It is applicable only when there is in reality no profits or

gains; and it is not used for calculation of loss. The general principle is that the diminution of value of buildings, machinery, plant and furniture should be taken into account in calculating the result of the year's working; for the sake of convenience a certain percentage of the original cost is taken to represent the diminution in value during the year. There is no reason why this general principle should not receive full application in calculating the loss of profits or gains. Every business-man will consider whether the machinery and furniture used for his business have become less valuable when he is calculating the result of the year's working. Again, suppose that the profits of a business computed after making the allowance detailed in section 10 amount to Rs. 1,000: surely, if the income had been Rs. 2,000 less and the expenses had been the same, there would have been a loss of Rs. 1,000.

6. In my opinion the question must be answered in the affirmative

7. I add that the reasoning in *Arunachalam Chettiar v. The Commissioner of Income-tax, Madras*(1), would involve an answer, qualified but to a great extent in the affirmative, to the question on other grounds. The learned Judges who decided that case considered that a partner of a firm, registered or unregistered, which carried on business, was an assessee in respect of the profits or gains of that business and was therefore entitled to set off the loss in the business of the firm against the profits in other business carried on by him. I respectfully dissent from this reasoning. As I have pointed out, it is clear that a registered firm can be an assessee. The firm, then, is the assessee in respect of the profits and gains of the business of the firm. A partner is not assessed with regard to the profits of the firm and is therefore not an assessee. It is only under the provisions of section 24 (2) that a partner in the firm is allowed to set off against the profits, for which the partnership is liable to pay income-tax, a proportion of the loss incurred by the firm. Costs will be paid by the Commissioner. Counsel's fee one hundred rupees.

(343) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Sir Courtney Terrell, Kt., Chief Justice, Mr. Justice Das
and Mr. Justice Kulwant Sahay.

(25th November, 1929).

J. M. Casey

.. Assessee.*

v.

The Commissioner of Income-tax, Behar and Orissa .. Referring Officer.

*Indian Income-tax Act (XI of 1922), Sec. 2 (1) (b) and 4 (3) (viii)—
Cultivation of aloe plant—Sisal fibre, manufacture of, by machinery—Income,
if agricultural income.*

The assessee prepared sisal fibre for sale in market by means of machinery from aloe plants cultivated by him. It appeared that there was no cultivation of the aloe plant save in connection with the economic process involving the use of machinery such as was employed by the assessee, barring the laborious and un-economic process employed by the Jail authorities and that there was no market in the proper sense of the word for the aloe leaves.

(1) 1 I.T.C. 278.

* (1930) 1 L.R. 9 Pat. 185; A.L.R. (1930) Pat. 44.

HELD, that the whole of the profits derived from the manufacture of sisal fibre was agricultural income within the meaning of section 2 (1) (b) of the Act and as such exempt from assessment to income-tax.

Case [Miscellaneous Judicial Case No. 82 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Behar and Orisa, for the opinion of the High Court.

CASE.

Mr. J. M. Casey, the applicant in this case, derives his income from the sale of oranges grown on an orange plantation in Sambalpur District, the income of which has not been taxed as being purely of an agricultural nature, and from the growing of sisal hemp plant on a plantation of several hundred acres the leaves of which are carried to his factory by lorry and there passed through a machine called a decorticator which strips the pulp from the leaves and leaves the fibre.

2. Mr. Casey was assessed for the first time in the year 1927-28 on an income of Rs. 2,975 derived from what the Department held to be the non-agricultural part of this business in the year 1926-27, and under Sec. 34 on an income of Rs. 8,425 on the escaped income of the year 1925-26. No assessment was made in previous years as the existence of this business was not known to the Department until that year (1927-28). The assessee raises no serious objection to the method adopted by the Department for separating the industrial profits of the concern from the agricultural profits on the assumption that some part of the profits is non-agricultural, but he does raise the contention that no part of the profits is non-agricultural.

3. The sisal hemp plant from which the hemp fibre is manufactured in this case is very similar to the ordinary aloe plant, though it belongs, I believe, botanically to a different class. The leaves are cut and then transported by lorry to the factory where they are passed through a decorticator. The fibre is then washed in troughs to remove the pulp which may still be adhering. It is then dried on racks in the sun, baled in a bailing press and despatched to the rope factories in Calcutta or elsewhere. The prime mover in the factory is a steam boiler which cost the assessee Rs. 2,000 second-hand. The decorticator which was made by Krupps the well-known German firm cost a little more than £1,000 new and was purchased second-hand by the applicant for rupees 5,000. The leaves when brought into the factory are placed on an endless tray along which they move until they come in contact with knives fixed on a drum the axis of which is at right angles to the endless tray. These knives beat or strip off the pulp from one side of the leaves and then as the result of an automatic reverse motion the leaves again come into contact with these knives and the other side is stripped clean. The pulp drops down while the fibre is delivered at the far end of the machine.

4. The question which arises for the decision of their Lordships, in this case, is whether any part of the profits resulting from the growing of sisal hemp and manufacture from the hemp plant of fibre is taxable, or whether, on the other hand, the whole of the profits are exempt as being purely agricultural income.

5. Under Sec. 2, clause (1), sub-clause (b) of the Act, agricultural income includes income derived from agricultural land by the performance by a cultivator of any process ordinarily employed by a cultivator to render the produce raised by him fit to be taken to market, and under Sec. 4, clause (3) sub-clause (viii), agricultural income is exempt from tax.

6. As I am required by Sec. 66 of the Act to state my own opinion on the point raised, I do so below.

7. The question at issue really appears to be whether the process employed by the applicant in this case is a process ordinarily employed by a cultivator to render the produce raised fit to be taken to market and this would appear to be in reality a question of fact as stated by Atkinson, J., in the case of *Bhikanpur Sugar Concern*(1).

8. Assessee contends that there is no market for the raw leaf itself, but this is hardly correct. It will be seen from the affidavit of the Jailor of the Ranchi jail, a copy of which is annexed to the statement of the case and marked A*, that aloe leaves are purchased by the jail authorities at Re. 1 per cartload apart from cartmen's wages, and from the affidavit of the Jailor of the Motihari Jail, a copy of which is annexed and marked B*, that aloe leaves are purchased by the Motihari jail at cost of 0-4-0 to 0-8-0 per hundred leaves. It is not correct therefore to state that the leaves themselves before manufacture have no value.

9. Again, the process of manufacture adopted by the assessee in this case is different from the process adopted in these jails or by the ordinary villagers who some times beat out the fibre for the purpose of making ropes. The assessee uses comparatively expensive machinery, while in the jails and villages the leaves are stripped by hand and the pulp removed by a process of beating by wooden mallets.

10. In my view therefore the raw leaf has a market value but if assessee's contention that it has not is correct, this does not help his case. In fact, it does exactly the opposite, for it proves that the whole of his profits are industrial and not part industrial and part agricultural.

11. Section 59 of the Act read with Statutory Rule 23 makes it clear that the law has provided for cases in which income is derived partly from agriculture and partly from business. Again, the discussion in the Council of State and the Legislative Assembly at the time this bill was before the Legislature on the correct interpretation of the expression 'agricultural income' as defined in Sec. 2 clearly indicates that taxation of the non-agricultural profits in such cases was intended. I quote below from the speech of the Hon'ble Mr. Moncriff Smith as reproduced at p. 21 of Iyengar's Law of Income-tax. "The clause, as it will be amended now, will enable a landholder or a cultivator to sell his produce provided he has not employed in regard to that produce any process other than the process referred to in the preceding sub-clause, that is to say, he will be able to employ a process which will enable him to take it to market for sale but will not be allowed to perform any further process, otherwise the income which he derives from the sale will be liable to pay tax under this Bill." Again, Mr. G. G. Sim is quoted at p. 24 of this Volume as saying "It was desired to make it perfectly clear that where a person sold the raw produce of his land after it had been worked up by a process other than the process described in sub-clause (2), it should still be the case that the profits of the working up are profits liable to income-tax; otherwise it would not be possible, for example, to tax the profits from running a sugarcane factory where the owner of the factory gets the cane from his own land. Similarly, in the case where a man has a rice milling factory, we must still tax the profits of the

(1) 11. T. C. 83

* Not Printed.

milling..... The rule that has always been in force is this that where a man works the factory which is entirely supplied with the produce of his own land, we deduct as a business expense the whole of the value of the raw material, that is to say, the value that it would fetch in the open market."

12. In my opinion then the profits of applicant's business in this case are partly agricultural and partly industrial and he is legally liable to tax on the industrial portion of his profits; for the process of manufacture employed by the applicant in this case is not the performance by a cultivator of any process ordinarily employed by a cultivator to make the produce fit to be taken to market. The only process ordinarily employed by a cultivator to render the produce fit for the market is the mere cutting of the plant, while, in the case of the assessee, the plant after being cut is decorticated (and the fibre extracted and not the plant itself is sold).

M. Yunus, for the Assessee.

C. M. Agarwalla, for the Crown.

JUDGMENT

COURTNEY TERRELL, C. J.:—This is a case stated by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act, XI of 1922.

The assessee among other activities of an agricultural nature cultivates aloe plants and from them by means of machinery prepared sisal fibre which he sells in the market. The Department do not claim to recover tax on such portion of his profits as is attributable to the production of the aloe leaves but it is contended that the manufacture of the fibre from these leaves constitutes a manufacturing process as opposed to an agricultural process the profits from which are not exempt as agricultural income under section 4 sub-section 3 (viii).

The aloe plant from which the assessee produces the fibre is one variety of a class of plants indigeneous to India and growing freely in the wild state. The principal use of these aloe plants is to provide hedges but hitherto they have not been the subject of regular cultivation. It has long been known that the leaves of some varieties could be so treated as to yield a fibre suitable for the manufacture of rope and matting and villagers have occasionally been found to take the leaves of the wild plant, and by the use of a very rough and laborious process to extract fibre therefrom, but until suitable machinery could be devised for the purpose it has not been an economic proposition to cultivate the plant for the purpose of producing the fibre. In short the cultivation of the plant had to await the introduction of a process for producing the fibre therefrom on an economic scale. When this had been accomplished the deliberate cultivation of the plant and the selection of good varieties became profitable and in British East Africa and some other parts of the world it has become a regular industry. In India, however, it has until now assumed very small proportions and the assessee is one of the pioneers of the enterprise.

The contention urged by the Department is that the agricultural part of the industry terminates at the production of the leaf and its cutting and carting. Now under section 2 (1) (b) of the Act agricultural income means "Any income derived from such land by (i) agriculture, or (ii) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received

by him fit to be taken to market, or (iii) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, in respect of which no process has been performed other than a process of nature described in sub-clause (ii)''.

The question for our decision is whether any part of the profits resulting from the growing of sisal and the manufacture from it of the fibre is taxable, or whether, on the other hand, the whole of the profits are exempt as being purely agricultural income. Now it is perfectly clear from the wording of the section that an agricultural process does not necessarily stop short at the removal of the plant from the soil. In the case of , for example, cereals plants they must be threshed and winnowed in order to produce the grain and the process of threshing and winnowing is one ordinarily employed by the cultivator to render the produce fit to be taken to market. It is further to be noted that in order to test whether the process employed by the assessee is an agricultural process it should be possible to compare it with that which is "ordinarily employed by a cultivator", that is to say, it must be found that the plant with which we are concerned is in fact cultivated and that the cultivator in order to render the produce fit to be taken to market ordinarily employs a process to treat the produce of actual cultivation.

Now in this case there is in the first place no cultivation of the aloe plant save in connection with the economic process involving the use of machinery such as is employed by the assessee and therefore the process "ordinarily employed" is in fact that used by the assessee. In spite of the enquiries which the Department has been able to make nothing in connection with the cultivation of aloe fibre has been discovered save that aloe leaves are bought by certain jail authorities from persons who cultivate it and supply the leaves to the jail, the jail being apparently the only market which such cultivators have for the disposal of their leaves. The leaves so bought by the jail authorities are treated by the prisoners by means of the same laborious and uneconomic process which is employed by some villagers in treating the leaves of the wild and uncultivated plant. The object of the manufacture in jails is not the conducting of an economic process which shall render profitable the cultivation of the aloe plant but merely to keep the prisoners employed on sufficiently laborious and punitive work. In other words this instance relied on by the Department does not provide a standard of comparison for the process employed by the assessee. The word "market" in the section implies a real centre of economic exchange and the purchase by jails is merely an artificial condition having no relation to a market for agricultural produce.

The Department rely upon the decision of the Calcutta High Court in the case of *Killing Valley Tea Company Ltd., v Secretary of State for India*(1). That case was concerned with the state of affairs in connection with the manufacture of tea. The assessee employed a process of manufacture applied to the leaf which involved the use of costly machinery and was of a complicated nature but the Court was able to compare this process with a process which had ordinarily been employed by the cultivators of the tea bush before modern manufacture has been introduced, that is to say, the dry leaf had long been known as a marketable commodity and the preparation of the dried leaf in its market form had been carried on by known processes of a simple nature. Here the standard of comparison was available and the modern manufacturing process could be clearly differentiated from it. But in the case of sisal fibre no such

(1) 1 I. T. C. 54

standard of comparison is available firstly because other than the so-called jail manufacture no cultivation of the sisal aloe plant appears to have been practised save in connection with the modern process of manufacture of the fibre and such manufacture of the fibre as had in earlier days been practised had not been associated with the cultivated plant but with the wild as casually found. Further there is no market in the proper sense of the word for aloe leaves. A fact may be noted in connection with the affidavit sworn by the jailor of the Motihari Jail which is indicative of the small extent to which the cultivation of the aloe plant is understood. The jailor uses the words "aloe fire" as synonymous with the word "sunn". Now it is well known that *sunn* fibre is produced from a plant which has no affinity whatever with the aloe plant. The manufacture of *sunn* fibre is a well understood and entirely distinct industry.

The conclusion at which I arrive is that if a generalisation may be made from the single instance available, then process ordinarily employed by the cultivator of the aloe plant in order to render his produce fit to be taken to market is that in fact employed by the assessee and the whole of the profits derived by him from the manufacture of sisal fibre is agricultural income and as such is exempt from taxation. It may be that in the future the economic conditions may change. If the growth of the aloe leaf should become established as an agricultural industry by itself, and if the manufacturers of sisal fibre cease to cultivate the plant themselves and should purchase the leaves in an open market, then such circumstances may possibly require re-consideration in the light of the income-tax law; but the circumstances which at present prevail, in my opinion, require that the question put to us should be decided in favour of the assessee. The assessee is entitled to his costs of this reference. Hearing fee 5 gold mohurs.

DAS, J.:—I agree.

KULWANT SAHAY, J.:—I agree.

(344) IN THE HIGH COURT OF JUDICATURE AT PATNA

Before Sir Courtney Terrell, Kt., Chief Justice, Mr. Justice Das and Mr. Justice Kulwant Sahay.

(25th November, 1929)

Rajniti Prasad Singh and another

Assessees.*

vs.

The Commissioner of Income-tax, Bihar and Orissa

Referring Officer.

Indian Income-tax Act (XI of 1922) Sec. 2 (1) and 8—Simultaneous mortgage and lease back to mortgagor—Transaction, if amounts to usufructuary mortgage—Interest received, if exempt as agricultural income—Income from Government securities—Sums paid to Vendor as interest accrued prior to sale—Collection charges—Deductability.

* (1930) I. L. R. 9 Pat. 194; A. I. R. (1930) Pat. 33.

In respect of a loan advanced by the assessee two documents were executed simultaneously, one purporting to be a usufructuary mortgage of certain villages, the other purporting to be a lease from the assessee to the mortgagor of the same villages. It appeared from the terms of the documents that the intention of the parties was that the assessee (mortgagee) was not to enter into possession of the mortgaged property, nor to enjoy the usufruct or receive the rents and profits from the property or to appropriate them in lieu of interest or in payment of the mortgage money. The mortgagor was to remain in possession of the mortgaged property and to pay the Government revenue while the assessee was to receive nothing but the specified rate of interest upon the loan.

HELD, that the transaction was not a usufructuary mortgage but a simple mortgage, the two deeds constituting one single transaction and that the interest under the deeds paid to the assessee during such period as he was not in possession of the villages was assessable to income-tax.

On an assessment of interest from Government securities sums paid by the assessee to his vendor equivalent to the amount of interest between the last date of accrual of interest and the actual date of sale of the security and the cost of collecting the interest on the securities cannot be deducted.

Case [Miscellaneous Judicial Case No. 73 of 1928] stated under Sec. 66(3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bihar and Orissa in compliance with the order of the High Court, dated 3rd August, 1928.

CASE.

This is the statement of a case under Sec. 66(3) of the Income-tax Act (XI of 22) on three questions of law submitted, as directed your Lordships in your order, dated the 3rd August 1928 in M.J.C. No. 73 of 1928.

2. The assessment out of which this reference arises was made by the Income-tax Officer, Monghyr, in the year 1926-27, on the income of the assessee for the 'previous year' ending 30th Phagon 1982-S (corresponding to February 1926) and the assessed income as computed by the Income-tax Officer was made up as follows:

	Rs.
(1) Securities tax free	1,490
(2) Securities not tax free	13,860
(3) Interest	78,513
(4) House property	5,836
(5) Other sources	1,000

3. On appeal the Assistant Commissioner reduced the income under the head 'Interest on securities' by the sum of 2,297 but granted the assessee no other relief. The assessee then filed before me a combined application under Secs. 33 and 66(2) of the Act. After hearing that application and after calling on the assessee to show cause why the sum of 2,297 allowed as an admissible deduction by the Assistant Commissioner should not be added back and after hearing him in this matter, I passed an order adding back this sum but allowing the assessee's contention in respect of a sum of 1,000 which the Income-tax Officer had computed as income from sairat, and, at the same time, I declined to make any reference to the High Court on any point of law. The assessee then moved your Lordships direct under Sec. 66(3) and your Lordships have directed me to state a case on three questions.

4. The first of these questions as formulated in the assessee's petition under Sec. 66(3) and accepted by your Lordships runs as follows: "Whether in law the income received by a mortgagee from a usufructuary mortgagor on account of his giving the mortgaged properties in lease to the mortgagors during the pendency of the term of the usufructuary mortgage is assessable to income-tax".

5. The facts out of which this question arises are set out below:—

6. The assessee had on the 9th January, 1924, lent a sum of 1,06,000 to one Deonath Sahai on the security of a usufructuary mortgage of the proprietary interest of the mortgagor in certain villages and on the same date he leased back these lands to the mortgagor, the latter agreeing to pay the assessee annually a sum of 10,533-12-0 while the debtor also bound himself to pay land revenue to Government. As stated above, the usufructuary mortgage and the lease returning the land to the debtors were executed on the same date and it is to be noted that the amount which the debtor agreed to pay to the assessee worked out exactly at 9-15-0 per cent. annually, on the sum advanced. As this case is exactly parallel to the case of *Subramanya Sastrigal v. Commissioner of Income-tax, Madras*(1) in which the Madras High Court held that such income is not agricultural income and as there was at the time at which I passed this order no contrary ruling published, I did not think it necessary to state a case on this point to your Lordships. The position has altered however by reason of the Full Bench finding of the Madras High Court in the case of *T. K. S. Ibrahimsa Ravuttar v. Commissioner of Income-tax, Madras*(2), and of the Allahabad High Court decision in *Mukkund Sarup v. The Commissioner of Income-tax United Provinces*(3), where it has been held that such income is agricultural income and is therefore not taxable.

7. I have stated the facts of the case above and I now proceed to express an opinion on the question raised as required by Sec. 66 clause (3) read with clause (2) of the Act.

8. I would respectfully submit that in a case of this sort, it is necessary to look to the essence of the transaction and that in this case where the assessee primarily pursues the profession or vocation of a money-lender, it should be held that the mortgage and lease back are merely devices to make assessee's capital more secure. Further, the question of double taxation in this case does not arise, for it is the mortgagor and not the mortgagee who pays land revenue and other Government dues.

9. In my view the facts of this case can be distinguished from the facts in the Madras case in *Ibrahimsa Ravuthar v. The Commissioner of Income-tax, Madras*(2), for in that case it was assumed that there was no stipulation as to interest in the usufructuary mortgage. I have been unable to secure the original mortgage bond and lease back and these will be submitted to your Lordships later, but in the meantime I have been supplied by the assessee through the Income-tax Officer with a rough translation of these deeds and the following extracts from the mortgage deed show that there is in that deed a stipulation regarding interest.

10. (Extract from para 5 of mortgage deed): "But the said creditor is not willing to advance debt (sic) unless sudhbharna is given of the properties noted below, and he demands interest at 0-13-3 per cent per mensem for the said debts and no other creditors are ready to advance loan at less interest."

(1) 2 I. T. C. 152.

(2) 3 I. T. C. 83.

(3) 2 I. T. C. 495.

11. (Extract from para 7): "Therefore, out of our free will, we the executants, having taken debt of Rs. 1,06,000 half of which would be fifty three thousand rupees at an interest of 0-13-0 per cent. per mensem, from Rai Bahadur Balmiki Preshad Singh (the mortgagee) *****.

12. (Extract from para 8): "That the annual interest of the said debt comes upto Rs. 10,533-12-0. In lieu of the said sum having fixed the annual rental at rupees 10,533-12-0 after giving deduction of collection charges and the Government demands, we the executants gave in Sudhbharna*****".

13. (Further extract from para 8): "Now the said Rai Bahadur getting in (sic) possession of the sudhbharna properties since the date of execution of this document should enjoy in lieu of interest the income Nakdi and Bhauli *****."

14. Further, in para 15 of the mortgage bond, it is stated that in case of payment of Rs. 1,000 or more than Rs. 1,000 within the term of this Sudhbharna deduction shall be made at the time of account year after year of the interest of the same at the rate of 0-13-3 per cent. per annum from the rental of this lease; and this same stipulation is repeated in the lease back to the mortgagor.

15. I would respectfully invite your Lordships' attention to the judgment of the Privy Council in the case of *Dewan Bahadur Ramarayanimgar, vs. Sri Rajah Velugoti Govinda Krishna Vachendra Bahadur Varu*(1), in which it was held that in similar circumstances a mortgage deed and lease deed should be read together as they formed parts of one transaction, the lease being in the nature of a machinery for the purpose of realising the interest. I respectfully submit therefore that the view expressed by Jackson, J., the dissenting Judge in the Madras case of *T. K. S. Ibrahimsa Ravuttar v. The Commissioner of Income-Tax, Madras*(2), referred to above, is the correct view and that viewed as a whole, the transaction is one by which a money-lender secures interest on the money advanced, that there was no real transfer of possession and the so-called rent has nothing to do with agricultural purposes, being based entirely upon the assessee's rate of interest.

16. The second question as formulated by the assessee and accepted by your Lordships runs as follows:—"Whether a sum paid by the vendee of Government securities to the vendor equivalent to the amount of interest due to the latter from Government on account of interest between the last date of accrual of interest and the actual date of the sale of securities at his own convenience and to facilitate the withdrawal of interest and quite apart from the sale price fixed for the securities, is assessable to income-tax and super-tax".

17. The facts out of which this question arises are as follows:

The assessee had purchased Government securities of the face value of one lac on various dates all falling within the period of 27th August 1925 to 22nd October 1925. In his books of accounts he showed separately what he called the cost of these securities and the interest due in the case of each block purchased from the last date on which interest was paid to the vendor upto the date on which he (that is, the assessee) purchased these securities and he claimed that this interest should be allowed as an admissible deduction from the interest drawn by him subsequently on those securities, and the Assistant Commissioner accepted this contention. He i.e., the Assistant Commissioner grasped the fact that amount so-called of interest prepaid is not and cannot be an item

(1) (1927) I. L. R. 50 Mad. 180,

(2) (3) I. T. C. 88.

of allowable expenditure under Sec. 8, but he came to the conclusion that this portion of the interest which was prepaid to the seller was not income of the assessee at all. He held that it was the receipt of the vendor and was assessable in the vendor's hand. As I was of opinion that the Assistant Commissioner had not correctly interpreted the law, I added back this sum (2,297) under Sec. 33.

18. I presume that in the question of law as formulated the expression "last date of accrual of interest" means "last date of receipt of interest" or "last date on which interest was receivable by the vendor" and I would at the same time urge that the expression "quite apart from the sale price fixed for the securities" in the question of law as formulated by the assessee can have no real meaning, for whether the amount of interest which had accrued from the last date on which interest was paid to the vendor upto the date of sale of the securities to the vendee is or is not calculated separately the total which the vendee pays to the vendor is and must form the sale price of the securities. If assessee can claim this sum as an admissible deduction from his total income he can do so only because it is in the first place an admissible deduction from his interest on securities. If we turn, however, to the relevant sections of the Act we find that while certain deductions are allowed in the case of income from property (Sec. 9.) income from business (Sec. 10), income from professional earnings (Sec. 11) and income from other sources (Sec. 12), in the case of interest from securities (Sec. 8), no deductions are allowed. The transaction in question is, in my view, a capital transaction and the purchase price of the securities is the total price paid including the amount by which the securities have appreciated as the result of accrual of interest up to the date on which assessee purchased them and what the assessee paid the vendor on this account is not interest on Government securities or any other kind of interest. Interest on securities is payable only by certain officers of Government and is taxable only in one manner that is, by deduction at source by the officer who pays it and the prospective recipient cannot pass on such interest before he has actually received it, and the sum received by the vendor is not interest and is not taxable in his hand: *Wigmore (H. M. Inspector of Taxes) v. Thomas Summerson and Sons, Ltd.*(1)

19. I understand that your Lordships' direction to state a case on this point does not prejudice the right of the Crown to object to the maintainability of the application in regard to this question.

20. As explained above the Income-tax Officer added back this sum to assessee's profits. The Assistant Commissioner allowed the assessee's contention while I, under Sec. 33, cancelled the Assistant Commissioner's order on this point and restored the assessment. In this connection, I would respectfully submit that your Lordships have no jurisdiction to issue a rule under section 66(3). That sub-section runs as follows:—“(3) If on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may apply within six months from the date on which he is served with notice of the refusal to the High Court, and the High Court if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it and, on receipt of any such requisition, the Commissioner shall state and refer the case accordingly.” Your Lordships' jurisdiction would appear to arise only after the assessee has on any point asked the Commissioner to state a case under section 66 (2) on any points arising out of an appellate order and the Commissioner has refused to do so. In this case, I was not asked by the assessee under that sub-section to state a case on this point and section 66(3)

has in my view no application. It is true that I could *meo motu* state a case under Sec. 66 (1), but as assessee's contention in this matter appeared to me to be completely without substance, I did not do so. Assessee can ask for rule under Sec. 66 (3) only if the following conditions are fulfilled: (1) If he has made an application under Sec. 66 (2) accompanied by a fee of Rs. 100 (2) If the question raised is a question of law (3) If that question arises out of the appellate order. In this case, assessee has made no such application and while the question is in all probability a question of law, it cannot be held "to arise out of the appellate order." That expression must mean that the appellate order is the immediate cause or occasion out of which the question of law arises, but, in this case, the question arose as the result of my order passed under Sec. 33 and would never have arisen if I had not passed that order. It may be argued that if this view is correct the results are anomalous and it is always possible to circumvent an assessee and prevent him from making an application to the High Court on a question of law. It does not follow, however, that because the result is anomalous, the law has *ex-hypothesis* been wrongly interpreted and this argument is based on the assumption that officers of the department are prepared to act in a *mala fide* manner to defeat the ends of justice.

21. I do not see how it can be argued in this case that the point in question arose out of the appellate order, because the Assistant Commissioner had allowed the appellant's contention. But if this view is tenable, it would certainly be not tenable in circumstances where both the Income-tax Officer and the Assistant Commissioner had accepted the assessee's contention and the Commissioner had under Sec. 33 added back the item in question, though the results are exactly the same.

22. The sources of income and the amount of income under each head as computed by the Income-tax Officer is noted below:—

	Rs.
(1) Securities tax free	.. 1,490
(2) Securities not tax free	.. 13,860
(3) Interest	.. 78,513
(4) House property	.. 5,836
(5) Other sources	.. 1,000

The Income-tax Officer allowed a deduction of 5 per cent. from the gross income under the head 'interest', while he refused to allow any deduction or any percentage under the head 'securities'. In this connection, the question which has been formulated by the assessee and accepted by your Lordships is worded as follows: "Whether in law the basis of the establishment charges for the purposes of allowing percentage of deduction should be total income of the assessee excluding the amount of interest on securities, although the latter is taken into consideration for calculating the gross assessable income of the assessee."

23. Assessee derives a substantial income from Zamindari property as well as from interest on securities and money lending. He maintains a combined staff and does not show separately in his accounts the cost or proportionate cost of establishment engaged in activities the profits of which are taxed. Assessee's income from money lending is taxable under Sec. 10, if it is held to be income from business, and taxable under Sec. 12, if it is income from other sources. In the former case, he is allowed under Sec. 10 (2) (ix) any expenditure incurred solely for the purpose of earning the profits and gains, and in the latter case, an allowance is made in respect of any expenditure incurred solely for the purpose of making or earning such profits or gains, provided that no allowance can be made on account of personal expenses of the assessee. It is the assessee's

duty to prove what the admissible deductions are in either case and, as he has not done so, in this assessment, he has, in my view, no right whatever to claim any deduction and the 5 per cent. which has been allowed on income from money lending has been allowed only as a matter of grace.

24. Assessee, however, so far from being satisfied with this, claims that he should be allowed a percentage for establishment on his income from securities. Income from this source is taxable under Sec. 8 of the Act and under that section no deductions whatever are allowable.

25. Finally, I would respectfully submit that this question as formulated by the assessee is unhappily worded, for in law there are no percentages of deduction except in the case of income from property, and in the case of income from sources other than property percentages do not form the basis of calculating admissible deductions. In the case of income from interest on securities taxed under Sec. 8, no deductions are allowed and where income is derived from property certain deductions are allowed under the various sub-clauses of Sec. 9 (1), while, in the case of income from business, deductions are allowed under the sub-clauses of Sec. 10 (2), In the case of income from professional earnings, certain deductions are allowed under section 11 (2), and, in the case of income from other source similarly under Sec. 12 (2). The deductions claimed however under these various clauses must be specifically proved and assessee cannot, it is submitted, claim as a right any percentage of deduction on his income from money lending and he cannot claim either as a right or favour any percentage of deduction from his income from Government securities.

26. It is respectfully submitted therefore that all the questions formulated should be answered in favour of the Department.

K. P. Jayaswal, Manohar Lal and Bindhyeshwari Prasad, for the Assessee.

C. M. Agarwala, for the Crown.

JUDGMENT.

COURTNEY TERRELL, C. J.:—The first question for determination in this case is as to whether the income derived by the assessee by reason of a certain transaction is assessable to income-tax, or whether it is agricultural income exempt from tax by reason of section 4, sub-section (2) (viii) of the Income-tax Act, 1922.

The facts which gave rise to the transaction are as follows and are set forth in paragraph 6 of the statement of the case. The assessee had on the 9th January 1924 lent a sum of Rs. 1,06,000 to one Deonath Sahay and the parties executed two documents, one purporting to be a usufructuary mortgage of the proprietary interest of Deonath Sahay in certain villages, the other purporting to be a lease from the assessee to Deonath Sahay of the same villages. Each document recites the simultaneous execution by the parties of the other document and the two constitute a single transaction and must be so regarded and they must be construed together for the purpose of ascertaining the real nature of the transaction, as stated in the judgment of the Privy Council delivered by Lord Macnaghten in the case of *Abdullah Khan v. Basharatt Hussain* (1): "Their Lordships agree with the High Court in thinking that the mortgage and the lease were parts of one and the same transaction. But there is no inconsistency between the two instruments nor would there have been any inconsistency if the mortgage itself had contained a provision for granting a lease on the terms upon which the lease was actually granted".

(1) I. L. R. 35 All. 48 at p. 56.

It is contended on behalf of the assessee that although the documents must be considered as a single transaction yet they amount to a usufructuary mortgage and it is contended on the strength of two earlier decisions to be hereinafter referred to that the income of a usufructuary mortgagee as such is agricultural income and exempt from tax. Indeed the question formulated for decision by this Court is: "Whether in law the income received by a mortgagee from a usufructuary mortgagor on account of his giving the mortgaged properties in lease to the mortgagors during the pendency of the term of the usufructuary mortgage is assessable to income-tax?" As I shall point out having regard to the facts of the case this broad question does not arise and in spite of the weight of opinion in favour of a negative answer I would reserve my own views on the subject. It is enough for the purposes of this case to consider whether the nature of the transaction here involved was, when properly considered, a usufructuary mortgage, or whether it amounted merely to a simple mortgage in which case it cannot be denied that the interest stipulated for is assessable to income-tax.

The definition of a simple mortgage is contained in section 58 (b) of the Transfer of Property Act and one of the characteristics of a simple mortgage is the fact that possession of the mortgaged property is not delivered to the mortgagee. The definition of a usufructuary mortgage is contained in paragraph (d) of the same section and the essential features are that there shall be delivery of possession of the mortgaged property to the mortgagee with an authorisation to retain such possession until the payment of the mortgage money and to receive the rents and profits accruing from the property and to appropriate them in lieu of interest or in payment of the mortgage money or partly in lieu of interest and partly in payment of the mortgage money. Now the mortgage deed recites that the co-executants are members of a joint family and sets forth the parcels mortgaged. It recites that the executants tried their best to obtain a loan from several mahajans but have been unsuccessful. Paragraph 5 recites that "the said mahajan" (the mortgagee) "does not agree to advance the loan unless the properties noted below" (the parcels) "are given to him in mortgage. He demands the interest of the said loan at the rate of Re. 0-13-3 per one hundred rupees per month and no other mahajan agreed to lend money at a lower rate of interest than this." Paragraph 7 states that "For this reason we, the executants of own respective free will and accord, took a loan of Rs. 1,06,000 at an interest of Re. 0-13-0 per hundred per month from" the mortgagee..... "We the executants have received the whole and entire loan on account of this mortgage deed from the said mahajan." Paragraph 8 states "The annual interest on the said loan amounts to Rs. 10,533-12-0. In order to fetch an annual jama equal to the said sum we give in mortgage to..... the said mahajan the proprietary interest with all zemindary rights including the surface and sub-soil rights and irrigation and other rights in respect of" and then follows a fresh repetition of the parcels. Then in paragraph 9 it is said "The said mortgagee has and shall have the right to appropriate the enhanced jama which may be derived from the mortgaged village through his labour and diligence. We the executants neither have nor shall have anything to do with it." Paragraph 10 contains a covenant by the executants to pay the Government revenue on account of the mortgaged property and in the event of failure to pay the revenue if the property is sold by auction for arrears of revenue then the mortgagee is to have the right to realise the entire amount of the loan, principal with interest, after deduction of the sum already paid to him by selling by auction the mortgaged property and also by recovering it from them personally. In paragraph 11 there is a further covenant that in the event of the executants dispossessing the mortgagee from the mortgaged properties during the term of the mortgage the mortgagee may realise the amount of the loan

with interest by selling the property and also by recovering it from the executants personally. Paragraph 14 provides that the principal sum of the loan may be paid off in instalments of not less than Rs. 1,000 at a time and paragraph 15 recites that the executants have taken a lease from the mortgagee of the mortgaged property under another deed of even date at the annual rate of Rs. 10,533-12-0, and in the event of any reduction of the principal sum due by payment of instalments as provided by clause 14 the rent payable is to be reduced in proportion.

The lease which was executed on the same day sets forth the parcels of the leased property and shows (and it is not denied) that they are precisely the parcels covered by the mortgage deed. It recites the mortgage and states "It is desirable that we the Katkenadars (lessees) aforesaid in coming into and remaining in possession and occupation shall enjoy the usufruct thereof and pay to the Sudhbharnadar (mortgagee) aforesaid the rent fixed as above according to the kist bandi given below." If the rent is not paid according to the kist the lessees have to pay interest on the defaulted kist which the mortgagee-lessor shall have the right to realise from the lessees. If within the term of the lease the lessees pay off the recited mortgage debt then the mortgage bond is to be delivered back to them and the lease is to be cancelled and there is a further provision that if the lessees do not pay the rent according to the kist then the mortgagee-lessor is to have the right to oust the lessees from the leased property in the case of two kists remaining unpaid and shall realise the rent direct or may settle the property with another lessee. There is a further provision like that in the mortgage deed for the reduction of the rent if instalments are paid in discharge of the principal of the mortgage debt. The lessees also bind themselves to comply with the requests made by the mortgagee to submit to him the jamabandi account papers in the names of the tenants of the mortgaged villages when they shall be demanded by the mortgagee.

Now it is very obvious that the intention of the parties is that the mortgagee is not to enter into possession of the mortgaged property; nor is he to enjoy the usufruct of the property or to receive the rents from the property or to appropriate them in lieu of interest or in payment of the mortgage money. It is equally clear that the mortgagor is to remain in possession of the mortgaged property and it is the mortgagor who is to pay the Government revenue. The mortgagee is to receive nothing but the specified rate in interest upon the loan. The nature of the transaction must be discovered from the documents and the documents alone. It has been suggested to us that the usufruct of the mortgaged property must have been valued at the provided rate of interest, that is to say, Rs. 10,533-12-0 but there is no evidence of this and moreover even if it were true it would not be material. The nature of the transaction is not that of a usufructuary mortgage but that of a simple mortgage and the two deeds constitute one single transaction. The whole of the transaction might have been expressed in a single mortgage deed and the real and obvious reason for splitting it up into two documents is to enable the mahajan who is the assessee to put forward a specious claim to escape income-tax. Needless to say the mere fact that the transaction is a device to escape income-tax ought not to prejudice the assessee. Any subject of the State is entitled to escape paying taxes if he can devise a lawful method of doing so but by dividing what is in fact a single transaction between two documents he does not achieve the device which he seeks; nor does he change the nature of the transaction.

Two cases have been relied upon by the assessee which require some comment. The first is that of *Ibrahimsa Rowther v. Commissioner of Income-tax, Madras*(1), where a somewhat similar device had been successfully used for the

same purpose but one feature distinguished the facts of that case from the facts of that now under consideration, namely, that in the usufructuary mortgage no mention whatever was made of any rate of interest and in that respect the mortgage deed and the lease were inconsistent and could not be regarded as a single transaction. The documents are not set forth in the report but the fact I have stated is emphasised and at p. 37, Mr. Justice Srinivasa Ayyangar says "We must take it that the usufructuary mortgage referred to in question is a simple or pure usufructuary mortgage and that there is no stipulation as to any interest and that the income accruing from the properties mortgaged is to be taken and enjoyed by the mortgagee with possession."

The case of *Mukund Sarup v. Commissioner of Income-tax, U. P.*(1), is also a decision upon the facts of that particular case. The mortgage and the lease are not set forth in detail. It is true that the head note would seem to indicate that it is a decision that in the case of a lease back to the mortgagor with a stipulation for fixed annual payments amounting to a definite percentage of the sum advanced that the annual payments should be excluded from assessment but at page 499, Mr. Justice Sulaiman delivering the judgment with which the two other Judges concurred said: "It seems to me that to hold that such a person is liable to pay income-tax would amount to holding that the transaction is not that of a usufructuary mortgage but almost a simple mortgage. It is impossible to hold in this case that the transaction was not that of a usufructuary mortgage. No doubt the mortgage deed and the lease were executed on one and the same date and the cross-references in the two documents indicate that the whole transaction was settled at one time. Nevertheless there are certain distinguishing features which make the position of the present usufructuary mortgagee quite distinct from what it would have been if he had taken a purely simple mortgage. He has under the lease the right to recover rent through the revenue court, which very often, is a speedy remedy. He has also the security of the fixed amounts being paid to him regularly year after year, with the option of entering into possession on the default of such payment. If he enters into possession after the ejection of the mortgagor he is entitled to cultivate lands himself or to let the lands to tenants and receive profits from them. Under these circumstances it seems impossible to hold that the position of the assessee is that of a purely simple mortgagee who is liable to pay income-tax." It will be seen that the basis of the decision was that in the particular case in question the transaction did not amount to a purely simple mortgage. Mr. Justice Ashworth said at page 500, "Does it make any difference when by means of a lease, forming a single transaction along with the mortgage, the mortgagee restores possession to the mortgagor, and himself, in the form of rent, receives a sum equal to the land revenue plus interest at a definite rate? The answer to this depends on whether the result of the two deeds could have been effected *in toto* by a simple mortgage deed. My learned brother has shown that this was not the case. The result of the execution of the two deeds is fraught with consequences that would not attach to the execution of a simple mortgage deed. One transaction differs from the other not merely in form but in substance." This decision is therefore not in point.

I am constrained to say that even if the effect of the two deeds were as stated in the judgments of the learned Judges I should be inclined to differ from their conclusion that there were two separate transactions and that the ultimate result was not that of a simple mortgage but it is probable that the learned Judges found other circumstances in the transaction which justified them in their conclusion of fact and it is perfectly clear from the passages I have quoted that if they had decided that in fact the transaction was a single

one and in the nature of a simple mortgage, they would have held that the interest whether described as such or as rent would have been assessable to income-tax. I would answer the question propounded to a limited extent by stating that in the opinion of the Court the interest reserved by the documents in this case and paid to the assessee during such period as he is not in possession of the leased property is assessable to income-tax, leaving it open for future discussion as to whether the income of a usufructuary mortgagee is so assessable, and whether if the mortgagee lessor enters into possession the usufruct will be assessable.

The next question propounded by the Commissioner of Income-tax is concerned with the dividends drawn by the assessee upon certain securities purchased by him. It appears that the assessee had purchased Government securities of the face value of one lakh on various dates all falling within the period 27th August 1925 and the 27th October 1925. In his books of account he showed separately what he called the cost of these securities and the interest due in the case of each block purchased from the last date on which interest was paid to the vendor up to the date on which he (the assessee) purchased these securities and he claimed that this interest should be allowed as an admissible deduction from the interest drawn by him subsequently on these securities. It was argued before us on behalf of the assessee that in purchasing the securities he had paid a price which represented not only the capital represented by the securities but the dividends which would next fall due and therefore that that portion of the purchase price which represented the dividends went into the hands of the vendor and should be considered as the vendor's income. Now it has been held in England by Mr. Justice Rowlatt in the case of *Wigmore, (H. M. Inspector of Taxes) v. Thomas Summerson Sons, Ltd.* (1), that dividends do not accrue as interest from day to day but are receivable only on the day on which the holder of the security is entitled to draw them. Section 6 (ii) of the Indian Income-tax Act taxes "interest on securities". Section 8 states "The tax shall be payable by an assessee under the head 'interest on securities' in respect of the interest receivable by him on any security of the Government of India.....". The dividend is clearly receivable only by the holder of the security and it is not receivable until the date specified. In this case it was received by the assessee after he had become the owner and in these circumstances the section clearly provides that tax is to be levied in respect of the sum so received. The section has no concern with the profit or loss made by the assessee as a result of the investment of his money; nor is the section concerned with the rate of interest which the dividend provides for the capital invested by the assessee. The question as formulated runs as follows:—"Whether a sum paid by the vendee of Government securities to the vendor equivalent to the amount of interest due to the latter from Government on account of interest between the last date of accrual of interest and the actual date of the sale of securities at his own convenience and to facilitate the withdrawal of interest and quite apart from the sale price fixed for the securities, is assessable to income-tax and super-tax." I would answer this question in the affirmative.

It was, however, objected on behalf of the revenue authorities that the Court had no jurisdiction to entertain this question and that the Commissioner had been directed to state the case with an express reservation that he should be at liberty to take the preliminary objection on this point. It is contended that as the addition to the assessment had been made by the Commissioner in virtue of his powers of revision under section 33 that there is no power in the High Court to direct him to state a case with reference to such a revisional

order. There appears to be much authority in support of this contention though I would prefer to reserve my own view upon the matter for the situation is certainly very anomalous. In view, however, of my opinion that the revisional order was in law perfectly correct it is unnecessary to discuss the point of jurisdiction.

The third question is very simple. The assessee claims to deduct as part of his expenses a sum which he says represents the cost of collecting the interest on the securities. It is argued that the assessee is a minor and must in any case employ a bank or some other agency for collecting his dividends and the charges made by the bank for this service should be allowed as an expense. There is however no provision in the Act for the deduction of such expenses and section 10 provides for the deduction of expenses in respect of carrying on a business and sections 11 and 12 deal with allowable deductions in the case of professional earnings and other sources. The matter is moreover concluded by the judgment of this Court in the case of *Maharaja Guru Mahadeo Ashram Prasad Sahi Bahadur v. Commissioner of Income-tax, Bihar and Orissa*(1). In my opinion the deduction under the head "securities" is not allowable.

The assessee has been unsuccessful on all the points raised by him and he must pay the costs of this reference. Hearing fee Rs. 100.

DAS, J.;—This is a case stated by the Commissioner of Income-tax, Bihar and Orissa, under section 66 (3) of the Income-tax Act. The facts upon which the question of law arises are these: On the 9th January 1924 certain persons, who may be referred to as the Sahays, executed a usufructuary mortgage bond in favour of Balmiki Prasad Singh, the father of the assessee, to secure an advance of Rs. 1,06,000 and interest thereon at the rate of 13 as. 3 pie per cent. per month amounting to Rs. 10,533-12-0 per year; and Balmiki Prasad Singh on the same day gave a lease of the properties covered by the usufructuary mortgage bond to the Sahays at a rent of Rs. 10,533-12-0 per year. The Income-tax Officer took the view that it was open to him to assess income-tax on the sum of Rs. 10,533-12-0 admittedly received by the assessee from the Sahays during "the previous year"; and the question of law which arises on these facts has been formulated as follows by the assessee: "whether in law the income received by a mortgagee from a usufructuary mortgagor on account of his giving the mortgaged properties in lease to the mortgagors during the pendency of the term of the usufructuary mortgage is assessable to income-tax."

It is no longer open to doubt that under section 6 of the Income-tax Act, income, profits and gains from whatever source derived is chargeable to income-tax "save as otherwise provided by this Act." This is clear from the precise language employed in section 6 in which the different heads of income, profits and gains are specified. One of the heads is "other sources"; and section 12 specifically declares that the tax "shall be payable by an assessee under the head 'other sources' in respect of income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads)". The income in this case clearly comes within the sweeping words of section 12 unless indeed it is made out that it falls within the exceptions specified in the Act. Section 4 (3) provides that the Act shall not apply to certain classes of income and one of the classes of income excepted out of the Income-tax Act is agricultural income. 'Agricultural income' has been defined in section 2 as "(a) any rent or revenue derived from land which is used for agricultural purposes and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of Govern-

ment as such; and (b) any income derived from such land by (i) agriculture, or (ii) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market; or (iii) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, in respect of which no process has been performed other than a process of the nature described in sub-clause (ii)'. There is little doubt therefore that to claim exemption in this case the assessee must establish that the sum of Rs. 10,533-12-0 received by them is 'agricultural income' within the meaning of that term as defined in the Income-tax Act. It is impossible therefore for us to accept the broad contention which was advanced by Mr. Jayaswal to the effect that if the source from which the income arises is agricultural land, it is exempt from taxation. I have no doubt whatever that we have nothing to do with the determination of the question as to the source from which the income arises except perhaps for determining whether the income is agricultural income or not.

It was then contended by Mr. Jayaswal that the income in this case is agricultural income since it arises as the result of a usufructuary mortgage which entitled the assessee to retain possession of lands which were undoubtedly assessed to land revenue in British India and to recover the rents and profits issuing out of those lands, as the proprietor of the property for the time being. Whether the income derivable by a usufructuary mortgagee is or is not agricultural income within the meaning of that term as used in the Income-tax Act is a difficult question which I do not propose to determine in these proceedings. It may be urged that the common form of usufructuary mortgages is that in which the borrower says to the creditor, "You lend the money and I the land; if either of us wants that which he has lent he shall restore that which was lent to him"; and that the income derivable from a transaction so described is agricultural income, assuming that the land, which is the subject matter of the transaction is used for agricultural purposes and is either assessed to land revenue in British India or is subject to a local rate assessed and collected by officers of Government as such. On the other hand it may be urged with equal force that a mortgage does not cease to be a mortgage because possession is delivered to the mortgagee, and that the essence of a mortgage, simple or usufructuary, is that a loan is advanced and a security given for the due repayment of that loan; and that the income derivable by the mortgagee, whether in possession or not, is interest upon the money advanced and is the return from money, not rents, issues and profits from the lands mortgaged and therefore not a return from the land. As I have said the question is a difficult one upon which much may be said on either side. I will assume in this case that the profits from a usufructuary mortgage are outside the ambit of the Income-tax Act, though I must make it clear that I do not decide the question in the present proceedings and reserve to myself the fullest liberty to determine the point if, and when, it arises.

But in this case there was not only a usufructuary mortgage executed by the Sahays in favour of Balmiki Prasad Singh but there was also "a lease back," as it has been described by Balmiki Prasad Singh, to the Sahays; and the simple question for our determination is whether the two transactions taken together amount to an usufructuary mortgage. The answer to this question must depend on the solution of the problem as to what in fact was the transaction between Balmiki Prasad Singh and the Sahays.

I will first consider the terms of the usufructuary mortgage bond. I may mention that the bond appears to be in common form. It recites that

Rs. 1,06,000 was being advanced by Balmiki Prosad Singh to the Sahays at an interest of 13 as. 3 pie. per cent. per month. It states that Rs. 10,533-12-0 would be the annual interest payable by the Sahays to Balmiki Prosad Singh and it provides that "In order to fetch an annual jama equal to the said sum, viz., Rs. 10,533-12-0 the proprietary interest with all zamindari rights" was being given in sudhbharna to Balmiki Prosad Singh. It then provides that the mortgagee should appropriate "the income derived from Nakdi and bhaoli holding, kamat land, khudkasht and bakasht lands..... in lieu of interest"; and it makes the position perfectly clear that the "right to appropriate the enhanced jama that may be derived from the sudhbharna village" should belong to the mortgagee. I have no doubt that if there was nothing else in the transaction, it would be construed as an ordinary usufructuary mortgage under which the mortgagee has to enter upon into possession, and appropriate the profits in satisfaction of the interest; and it might then be urged that as the transaction contemplated that the entire profits of the land should go to the mortgagee in his right as a zamindar, the income derivable by him was agricultural income. But the usufructuary mortgage bond does not stand alone. There is a further document which, in my opinion, qualifies the meaning which might otherwise be attached to the usufructuary mortgage.

It is necessary for me to deal with the terms of the other document which is a kabuliat executed by the Sahays in favour of Balmiki Prosad Singh on the same day, that is to say, on the 9th January 1924. Now before dealing with this document, I may mention that the execution of the Kabuliat is already recited in the usufructuary mortgage bond. In paragraph 15 of the usufructuary mortgage bond, the mortgagors says as follows: "We the executants have taken from the said Mahajan katkena lease of the said sudhbharna property under another deed of this date at an annual jama of Rs. 10,533-12-0 with effect from the 12 annas kist of 1331 Fs. and 16 annas kist of 1332 to 1333 Fs. In case a sum of Rs. 1,000 or more is paid within the term of this sudhbharna deed then interest thereof at the rate of 0-13-3 per hundred rupees per month shall be deducted year by year from the katkena rent of the property at the time of rendering an account, and the said mahajan shall be entitled to get such amount of the jama in respect of the katkena property as will remain due after the deduction of the interest on the amount paid at the rate of 0-13-3 per hundred rupees per month". It will be noticed that the rent payable under the lease is the same as the interest due to the mortgagees under the usufructuary mortgage bond and there is a clear provision that "the interest thereof at the rate of 0-13-3 per hundred rupees per month" shall be deducted from the rent in the event of the mortgagors making part payment to the mortgagees to the extent of Rs. 1,000 or more at a time. Now the lease merely carries out the intention which has already been clearly expressed in the usufructuary mortgage bond. It provides that the rent of the properties demised should be Rs. 10,533-12-0 per year and it also provides that if there should be any default on the part of the lessees in paying the rent the lessor would have the power to enter upon possession and satisfy himself out of the rents and profits. It makes it perfectly clear that "after paying the rent fixed as above whatever profit shall accrue from the katkena properties is and shall be the right of these katkenadars and heirs and their representatives up to the continuance of this katkena". In other words, (and this is a very material point) whereas if the usufructuary mortgage bond stood alone the mortgagees would have been entitled to receive the whole of the profits from the mortgaged properties even if those profits exceeded the interest payable by the mortgagors, under the lease the mortgagees are entitled to the fixed payment of Rs. 10,533-12-0 per year which is the interest calculated on the sum advanced at 0-13-3 per cent. per month, the excess profits going to the mortgagors.

Now this is the transaction, and the question is—is the transaction taken as a whole one of usufructuary mortgage? What is the position? Under the two documents which I have just described the mortgagee does not enter upon possession of the mortgaged properties and is therefore not entitled to receive anything more than the yearly interest provided in the mortgage bond. It is true that if there be default in the payment of interest it will be open to the mortgagees to enter upon possession; but at the present moment the mortgagees are not in possession and they are not entitled to receive anything beyond the yearly interest provided in the mortgage bond. It is true that the parties describe the sum payable by the mortgagors to the mortgagees as rent; but I am of opinion that we have to look to the substance and not to the form of the transaction. I take it that the most important argument advanced in favour of the view that the income derivable by a mortgagee from a usufructuary mortgage constitutes his agricultural income is that the income represents not only the interest payable to the mortgagee but the whole of the rents, issues and profits derivable from the land. Now that argument cannot be advanced in this case. When the two deeds are read together as forming parts of one transaction, there is little doubt that the lease is in the nature of a machinery for the purpose of realizing the interest. What the mortgagee has in view is the realization of interest, not the appropriation of the rents, issues and profits from the lands mortgaged. In my view it is idle to contend that a transaction of this nature is one of usufructuary mortgage. In my opinion the transaction is one of ordinary mortgage with a power reserved to the mortgagee to enter upon possession and satisfy himself out of the rents and profits should there be a default in the payment of interest.

It is right that I should deal with two cases upon which reliance has been placed by Mr. Jayaswal. In *Makund Sarup v. Commissioner of Income-tax, U. P.* (1), a Full Bench of the Allahabad High Court decided that if a person carrying on a money lending business lends money in the course of such business on the security of lands of which he takes a usufructuary mortgage and if he immediately leases those lands back to the mortgagor with a stipulation for fixed annual payments which amount to a definite percentage on the sum advanced, these annual payments should be excluded from the assessment of the profits of the assessee as being 'agricultural income' within the meaning of that term as used in the Income-tax Act. The case of the Allahabad High Court may well have been decided on the facts of that particular case; but at the same time there is much in the judgment with which I confess I am unable to agree. The leading judgment proceeds on the assumption that double taxation is against the policy of the Income-tax Act. What his Lordship had in view was the fact that the mortgagee under the terms of the mortgage bond was liable to Government revenue and his Lordship thought that "to hold that he is liable to both Government revenue and income-tax would be imposing a double taxation which is against the policy of the Act." With great respect I am unable to agree with this view. I quite agree that there may be a presumption that the same tax should not be assessed twice on the same person; for instance in *Carr v. Fowle* (2), it was observed that the statute presumably did not intend that a Vicar should in effect pay the same tax (land-tax) twice on the same hereditament. As Rankin, J., (as he then was) points out in *Emperor v. Probbhat Chandra Barua* (3), "This is plain enough. Thus the income-tax is one tax and income assessed under one schedule cannot be assessed all over again under another". But there is no presumption that I know of that because a person

(1) 2 I. T. C. 495.

(3) 1 I. T. C. 284.

(2) (1893) 1 Q. B. 251.

has been assessed under one statute he is immune from taxation under another statute. The question has been discussed with great clearness and precision in the judgment of Rankin, J., in the case to which I have already referred and it is unnecessary for me to pursue the point.

In dealing with the question whether if a usufructuary mortgagee is not liable to pay income-tax, a mortgagee who at the same time leases back the mortgaged land to the mortgagor with a stipulation that there should be fixed annual payment calculated on the basis of the rate of interest agreed upon between the parties, Sulaiman, J., in the Allahabad case said as follows: "It seems to me that to hold that such a person is liable to pay income-tax would amount to holding that the transaction is not that of a usufructuary mortgage but almost a simple mortgage". It seems to me that the argument employed by his Lordship begged the whole question which was in debate before him. Once it was assumed that the two documents amounted to no more than a usufructuary mortgage pure and simple, the issue was determined and the question was solved; but, with great respect, the whole question is, does it not make a difference that the person lending money, without assuming the responsibility of a usufructuary mortgagee provides for payment of interest to him and stipulates that in certain events he would be entitled to enter upon possession of the mortgaged properties? With the utmost respect, this question was not faced in the Allahabad case to which I have just referred. As I have pointed out the transaction viewed as a whole amounts to no more than this that there was a loan, there was a security for the loan, and there was further a machinery for the purpose of realising the interest.

The other case to which reference was made, the decision of a Full Bench of the Madras High Court in *Ibrahimsa Rowther v. Commissioner of Income-tax, Madras*(1), proceeds on the view that what was agreed to be paid by the mortgagor was rent. As I have said, we have to look to the substance and not to the form of the transaction. In the case before us the rent agreed to to be paid is exactly the amount of interest payable under the mortgage bond and there is a specific provision that in the event of part payment of the principal amount, the rent would be automatically reduced. In my judgment there is a clear distinction between rent and interest. Rent is the return from land for the use of one's land and signifies the sum payable in respect of the use of land. Interest is the return from money for the use of one's money and signifies the sum payable in respect of the use of money. Rent issues out of the land demised; whereas interest is revenue derived from the money lent. The problem for our consideration is whether the sum of Rs. 10,533-12-0 received by the assesseees in the previous year was received by them by way of rent or by way of interest. Viewing the transaction as a whole, I have no doubt whatever that it was received by way of interest; and in my judgment the question propounded in the case must be answered in the affirmative.

There are two other questions, not as important as the one which I have just discussed, but which nevertheless require our consideration. It appears that the assesseees purchased certain Government securities of the face value of one lac of rupees on various dates all falling within the previous year. Now the interest on those Government securities did not accrue until after the purchases were made by the assesseees; but by arrangement between the assesseees and the vendors of these Government securities the assesseees paid the sum of Rs. 2,297 to the vendors as interest due to the latter upon the Government securities up to the dates of the sales thereof, and subsequently recovered those interests from the proper authority. The assesseees claimed before the Income-tax Officer that

the sum of Rs. 2,297 paid by them to the vendors of these Government securities should be allowed as an admissible deduction from the interest drawn by them subsequently on those securities and the Assistant Commissioner accepted the contention of the assesseees. The Commissioner of Income-tax however in the exercise of his power of revision held that the view taken by the Assistant Commissioner was not correct and he added back the sum of Rs. 2,297 under section 33.

Now upon this the question formulated by the assesseees runs as follows: "Whether a sum paid by the vendee of Government securities to the vendor equivalent to the amount of interest due to the latter from Government on account of interest between the last date of accrual of interest and the actual date of the sale of securities at his own convenience and to facilitate the withdrawal of interest and quite apart from the sale price fixed for the securities, is assessable to income-tax and super-tax". The question has been inartistically drawn; but there is no doubt as to what the assesseees mean. The learned Counsel appearing on behalf of the Commissioner of Income-tax contends before us that this question is not open to us having regard to the fact that it is a question which arises out of the order passed by the Commissioner under section 33 and not out of the appellate order. It is not necessary for me to deal with the question raised on behalf of the Crown as in my opinion, the question raised by the assesseees must be decided against them. It seems to me that section 8 of the Income-tax Act is conclusive so far as this question is concerned. That section provides that "the tax shall be payable by an assessee under the head 'interest on securities' in respect of the interest receivable by him on any security of the Government of India, or of a Local Government, or on debentures or other securities for money issued by or on behalf of a local authority or company"; and then follow certain provisos which need not be considered in this case. Now the interest was undoubtedly receivable by the assesseees; it has in fact been received by them. On what ground then can it be suggested that the income-tax authority acted improperly in assessing tax on this sum of money?

If I have understood Mr. Jayaswal correctly, he contends that the interest on these Government securities up to the date of the sales thereof was properly payable to the vendors of these securities and not to the assesseees; and that to suit the convenience of all the parties the assessee paid the whole of the interest due to the vendors up to the dates of the sales as indeed he was bound to do, and subsequently recovered them from the proper authority. In my opinion the argument rests on a fundamental misconception as to the true position. The interest on Government securities does not accrue from day to day but accrues on certain specified dates. It did not therefore accrue to the vendors of these securities at all, since they sold those securities to the assesseees before any interest accrued on them. It may of course be that the vendors did not agree to sell the securities except on terms that the purchasers paid them, not only the market value of the securities, but also in addition a certain sum of money calculated on the basis of the interest supposed to be due to them on the dates of the sales of the securities. But that was a matter between the assesseees and the vendors, and the assesseees might well have protected themselves by insisting that the amount of tax which would ultimately be payable by them should be deducted from the purchase money; but we are not concerned with that question in these proceedings. The contention of the assesseees must fail on the terms of section 8 of the Income-tax Act and I must accordingly answer the question in the affirmative.

The last question arises out of the refusal of the Income-tax Officer to allow any deduction or any percentage under the head "securities". The following question has been formulated by the assessee; "Whether in law the basis of the establishment charges for the purposes of allowing percentage of deduction should be total income of the assessee excluding the amount of interest on securities although the latter is taken into consideration for calculating the gross assessable income of the assessee". Now it may be pointed out that the Income-tax Officer allowed a deduction of five per cent. from the gross income under the head 'interest'; while as I have already stated, he refused to allow any deduction from any percentage under the head securities. Now section 6 specifically mentions the different heads of income, profits and gains chargeable to income-tax. It will be noticed that while there are clear provisions that the tax payable under the heads 'property', 'business', 'professional earnings' and 'other sources' is subject to certain allowances specifically mentioned in section 9, section 10, section 11 and section 12 of the Income-tax Act, there is no provision that the tax payable by an assessee under the head "interest on securities" in respect of the interest receivable by him on any security of the Government of India, or of a Local Government or on debentures or other security for money issued by or on behalf of local authority or a company should be subject to any allowance. In support of the view clearly taken by the Legislature in this matter the simplest of reasons may be advanced, namely, that ordinarily no expense is incurred by a person in drawing his interest on securities. In my opinion the question must be answered in favour of the Income-tax Department.

As the assessee has failed on every point they must pay the cost of this reference, hearing fee Rs. 100.

KULWANT SAHAY, J.:—Three questions have been referred to us in this case under section 66 (3) of the Indian Income-tax Act (1922).

The first question relates to the income derived by the assessee on account of the transaction of the 9th of January 1924. It is contended on behalf of the assessee that the document of the 9th of January 1924 executed by Deonath Sahay and others in favour of the assessee was an usufructuary mortgage and that the income derived by the assessee was agricultural income within the meaning of section 2 (1) of the Indian Income-tax Act and therefore exempt from taxation under section 4 (3) (viii). The real question for consideration therefore is whether the transaction amounted to a usufructuary mortgage and the income derived by the assessee was agricultural income. It is contended on behalf of the assessee that if the mortgage executed by Deonath Sahay had stood alone there could be no doubt that the transaction was of the nature of an usufructuary mortgage, and the fact that on the same date the mortgagee executed a lease back to the mortgagors of the mortgaged property did not in any way alter the nature of the transaction. There can be no doubt that the two documents, viz., the mortgage by Deonath Sahay and others and the lease back by the assessee were parts of the same transaction and the two must be read together as forming one transaction. It is necessary to examine the real nature of the transaction. Reading the two documents together as one whole, there can be no doubt that the intention of the parties was that the mortgagors should pay the interest on the mortgage money at the stipulated rate and that it was only in the event of default on the part of the mortgagors to pay the stipulated amount that the mortgagee was to take possession of the mortgaged property. Having regard to the nature of the transaction it is clear that the sum agreed to be paid by the mortgagors under the lease was the interest on the mortgage money and the stipulation was that it was only on default in payment of interest

that the mortgagee was to take possession of the mortgaged property. The transaction was very much similar to that of the mortgage in *Partab Bahadur Singh v. Gajadhar Baksh Singh*(1). In that case the stipulation in the mortgage deed was that until delivery of possession of the mortgaged property the mortgagor shall pay interest at the rate of 2 per cent. on the mortgage money and by a lease executed at the same time as the mortgage some of the villages forming the mortgaged property were leased to the mortgagor who thus became the tenant of the mortgagee and paid rent in lieu of interest. It was held by their Lordships of the Judicial Committee of the Privy Council that the interest referred to in the mortgage deed was only interest until possession was given of the mortgaged property and that the mortgagee after possession took the rents and profits instead of interest. It is thus clear that what the assessee receives from the mortgagor in the present case is interest on the mortgage money and that it will become the rents and profits of the mortgaged property only after the mortgagee takes possession of the mortgaged property.

I am of opinion that the income derived by the assessee in the year under consideration was interest and not agricultural income and was therefore liable to assessment. I would answer the first question referred to us to this limited extent. What the nature of the income would be if the mortgagee takes possession of the mortgaged property is a question which need not be considered at present and must be left open for consideration in future. The question whether the income derived by a usufructuary mortgagee is agricultural income and exempt from taxation or whether it is merely interest and liable to assessment is a question upon which I express no opinion.

The second question relates to the interest drawn by the assessee upon certain Government securities purchased by him. I agree with my Lord the Chief Justice in the answer he proposes to give to this question. I desire however to point out that income-tax upon the securities in question was deducted at the time of the payment of interest under section 18 of the Act. The assessee does not contend that he is entitled to a refund of that tax. The question, however arises in relation to the fixing of his income for the purposes of super-tax. Under sub-section (4) of section 18 all sums deducted in accordance with the provisions of the section shall, for the purpose of computing the income of an assessee, be deemed to be income received. Therefore, under this provision of the Act the tax deducted at the time of the payment of interest on the securities has to be added to the income of the assessee for the purpose of computing his income for the purposes of super-tax. The tax deducted was out of the income derived by him as interest on the securities. If the tax so deducted has to be added to his income it is clear that the interest out of which the tax deducted is added should also be added to his income in order to compute the same for the purposes of super-tax. It is clear that the assessee cannot claim any deduction on account of the payment made by him to his vendor as under section 8 no such deduction is allowable.

As regards the third question, I agree with my Lord the Chief Justice that the assessee is not liable to any deduction on account of expenses.

(1) 1, L, R, 24 All 521.

(345) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Sir Courtney Terrell, Kt., Chief Justice, Mr. Justice Das and
Mr. Justice Kulwant Sahay.

(25th November, 1929.)

Maharajadhiraj of Dharbanga

.. Assessee.*

v.

The Commissioner of Income-tax, Bihar and Orissa Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 10, 13, 23, 34 and 66—Death of assessee pending reference, effect of—Money-lending business—Payments by debtor—Appropriation as to principal and interest—Assessee's accounts unsatisfactory—Question, if one of fact—Appropriation by creditor in subsequent years—Creditor keeping amounts in suspense—Debtor's properties taken over in partial discharge of debt—Debtor executing fresh hand-notes for balance not discharged—Collieries—Arrears of minimum royalty of previous years, payment of, Deductability—Report called for by Commissioner hearing appeal—Right of assessee to be heard again—Signature of assessment order outside assessment area, validity of.

A reference under Sec. 66 of the Indian Income-tax Act must be decided by the High Court though the assessee died before the hearing, proceedings once commenced thereunder not abating on death.

Smith v. Williams, 8 Tax Cas. 321, Followed.

The assessee carrying on money-lending business used to record payments made by his debtors in a deposit or general register without allocation as principal and interest and from time to time made entries in interest ledger purporting thereby to appropriate a part or the whole of the payments to the satisfaction of interest. This interest ledger was not kept up-to-date, entries corresponding to the deposit ledger not having been made contemporaneously. The Income-tax Officer in the absence of any evidence as to appropriation took the payments recorded in the deposit register in the account year as interest where any particular payment did not exceed the amount due in respect of interest and made an assessment on the total of these payments added to the amounts shown in the interest ledger.

HELD, that having regard to the assessee's method of accounting the assessment was warranted by law, as the assessee must be presumed, in the absence of evidence to the contrary, to have appropriated the payments to discharge of interest.

The question whether or not the assessee's accounts do not disclose his true income is one of fact.

James Cycle Co. v. Commissioners of Inland Revenue, 12 Tax Cas. 103. Applied.

Per Kulwant Sahay, J.: A creditor is entitled to keep the amounts received by him from his debtor in suspense and where he bona-fide does so, he is not liable to assessment so long as the appropriation has not been made and the account not settled; but if it is found that the suspense account is not kept bona fide the Income-tax Department is entitled to find for themselves what was the amount received on account of interest.

* (1930) I. L. R. 9 Pat. 240; A. I. R. (1930) Pat. 81.

Where the assessee in the account year (1332 F.s.) entered in his interest ledger a sum of Rs. 1,40,107 as interest received in years previous to 1332 F.s. of which a sum of Rs. 80,000 had been assessed by the Income-tax Department in 1331 F.s. and claimed the balance as transfer entries not assessable and time barred under Sec. 34 of the Income-tax Act,

HELD, that having regard to the prior assessments on estimates on account of the unsatisfactory accounts of the assessee, the sum in dispute was never taxed as income appropriated as interest and not having been treated as non-taxable and excluded before, the assessment in the year where the appropriation was first made was legal.

Commissioners of Taxes v. Melbourne Trust, (1914) A. C., 1001 *Applied*.

Where the assessee having a large mortgage loan business did not keep his suit register in respect of these loans up-to-date and his accounts not disclosing his actual income, was assessed in previous years on estimates.

HELD, that the Assessing Officer was right in making an estimate of his income by adding a sum of one lakh to the amount admitted by the assessee.

Where the assessee took over from his debtor who owed him a sum of Rs. 32 lakhs as principal and Rs. 6,09,571 as interest, a colliery, shares, bills, the benefit of a decree, etc., at a valuation aggregating to Rs. 20,74,973 and the debtor executed fresh hand notes for the balance of Rs. 17,34,596.

HELD, that the real nature of the transaction was a discharge in part of the liability pro-tanto of the items taken over and a record of the liability still outstanding by the execution of the hand notes and the assessee could not be considered to have received interest assessable to income-tax.

Where the assessee paid arrears of minimum royalty accrued prior to his taking possession of a colliery taken over by him from his debtor, the amount so paid was deductible as liability in the nature of a charge discharged in the account year.

Where in an appeal the Commissioner of Income-tax, after receipt of a report of the Assessing Officer called for by him as to whether the assessee's accounts established a loss or not, dismissed the appeal without a further hearing of the assessee,

HELD, that as the report being of a negative character did not contain anything new there was no denial of natural justice invalidating the rejection of the appeal.

An assessment order signed at a place outside the area where the assessee is ordinarily assessable under the Income-tax Act is a valid assessment.

Case [Miscellaneous Judicial Case No. 40 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Behar and Orissa for the opinion of the High Court.

CASE.

The questions of law formulated below arise or are claimed by the assessee to arise out of the order on appeal passed by me, exercising the powers of an

Assistant Commissioner under section 5 sub-section 4 of the Act, when dealing with the assessment made by the Assistant Commissioner of Income-tax, Patna Range (hereinafter referred to as the assessing officer) exercising the powers of an Income-tax Officer under that same section and sub-section, in respect of the assessment made on the Maharajadhiraj of Darbhanga (hereinafter referred to as the assessee) in the year 1926-27 on the income of the year 1332 Fasli and ending in September 1925.

2. The Assistant Commissioner had made assessment on a sum of Rs. 37,24,198, which I had on appeal reduced by the sum of Rs. 3,87,023 by my order passed on 24th May, 1927.

3. In connection with the supplementary assessment made under section 34 of the Act on this assessee in the year 1926-27 the assessee has after the hearing of this appeal, but before the order on appeal was passed and signed, filed a suit against myself, the assessing officer and the Income-tax Officer, Darbhanga, suing all 3 of us personally and asking that an order of permanent injunction should be passed against us preventing us from realizing the amount assessed in that case on the ground that this supplementary assessment was made out of malice by the assessing officer and because assessee had refused to accede to overtures made by him demanding illegal gratification, while I am charged in that plaint with acting from motives of malice and in collusion with the assessing officer.

4. On these grounds assessee raises two questions of law, the first being "Was I personally competent to hear the appeal" and the second being "Whether the Assistant Commissioner was competent to make the assessment".

5. Assessee's contention appears to be based on a general principle of law that no man can be a judge in his own case. I may be personally interested in the civil suit arising from that supplementary assessment, but it is perfectly obvious that I am not personally interested in this case with which I am now dealing. Further, this contention was not raised by the assessee in the grounds of appeal and he cannot therefore raise this question now in an application under section 66 (2) as it does not arise out of the appellate order.

6. The civil suit referred to above was filed on the 2nd April 1927, while this assessment was completed by the assessing officer in January 1927. The question of the competency or otherwise of the Assistant Commissioner to make this assessment has not been taken in the grounds of appeal and has not been discussed in the appellate order and cannot therefore be raised at this stage. Finally, even if I had been personally interested in this case I should still have been forced to hear the appeal, as the law of income-tax contains no provision for the transfer of appeals in such cases. If then I was not competent to hear the appeal, no one was competent and the assessee could not have prosecuted his appeal at all. I am of opinion that, for the reasons stated above, these questions cannot now be legally raised and if they are raised should be answered in the affirmative.

7. On foot of two decrees passed in favour of assessee against one Damodar Das Burman, the debtor has been making regular payments over a number of years to the assessee all of which have been entered in assessee's deposit account while not a single item has been shown in the interest account. In the year 1332 the debtor paid the assessee two separate sums, one of Rs. 3,400 and the other of Rs. 2,78,000. The assessee has classified the former sum as interest though this item is not shown in the interest account, while of the sum of Rs. 2,78,000, interest portion as claimed by the assessee is only Rs. 18,816.

The amount of interest which has accrued on this debt upto the end of the year 1332 is Rs. 3,09,281, but out of the total payments made upto 1331 only a sum of Rs. 38,091 which was the receipt of 1331 was taxed upto and including last year. Assessee's contention is that as this payment of Rs. 2,78,000 is the final payment towards the satisfaction of the original decree it should be deemed to have been paid in satisfaction of the principal. He bases his argument on the statement of the assessing officer in his assessment order that it is the accepted principle of accountancy followed by the assessee to credit realisations first towards interest and then towards principal. Obviously, what the assessing officer means is that this is the practice followed when allocation is made in assessee's registers but in this particular case all former realisations had been shown merely in the deposit account and no allocation between principal and interest had been made.

8. In connection with this matter the question of law formulated by the assessee is as follows:—"Whether where the assessing officer has found that there is an accepted method of accounting the assessing officer is bound by section 13 of the Income-tax Act to act on such accepted method and whether the judgment of the assessing officer claiming that Rs. 2,59,184 was paid as interest and was liable to be assessed in that year was wrong and whether his decision is not in direct conflict with the first paragraph of section 13 of the Act". The assessing officer has found that there is an accepted method of accounting only when actual allocation as between principal and interest is made in the account books of the assessee and the question at issue should be re-drafted as follows: -- "In the circumstances of this case what portion of the amount received from Damodar Das Burman in the previous year is legally taxable".

9. Assessee's contention is that as this payment of Rs. 2,78,000 is the final payment towards the satisfaction of the original decree it should therefore be deemed to have been paid in satisfaction of the principal. He argues that under section 3 of the Income-tax Act taxes are to be assessed on the amount received in the "previous year" but that the assessing officer and the appellate authority are in this case attempting to justify the taxation of profits received in past years. Assessee objects to the device of calculating the whole interest which has accrued during the pendency of the loan and of then holding any payment as interest if it does not exceed the amount of such interest regardless of the fact that such sum was paid as principal or was allocated to principal. But under section 3 of the Act tax is not assessed on the amount received in the previous year but on the income, profits and gains of the previous year. Clearly in this case assessee did not consider payments received in former years as interest, for in that case he would have paid tax on them in those years and the procedure followed by the assessing officer in this case appears to be both logical and in consonance with the proviso to section 13 of the Act. I am of opinion therefore that the total sum of Rs. 2,78,000 received in the year from Damodar Das Burman is legally taxable and not merely the sum of Rs. 18,816 out of this sum as assessee contends.

10. In the year 1332 one Amar Nath Bose, a judgment-debtor made payment to the assessee of the sum of Rs. 1,38,955, out of which Rs. 20,000 was in that year transferred to the interest account, the balance being kept in the deposit account. In the interest account of this year the total amount shown against this debtor's name is Rs. 1,60,107, Rs. 20,000, of which is the sum referred to above while Rs. 1,40,107 represents a transfer from the deposit account of years prior to the year 1332. The assessing officer charged to tax in the year 1332 the sum of Rs. 1,60,107, i.e., the sum transferred to the interest account in the year 1332 less the sum of Rs. 80,000 which was taxed last year;

while still in deposit, while he also taxed the interest portion of the amount actually received in the year 1332 and which was kept in deposit in that year.

11. The question which arises for decision in this matter is: "What is the amount of profits or gains arising out of the payments made by this judgment-debtor legally taxable in this year".

12. Assessee's argument is that the sum of Rs. 1,40,107 which has been transferred to the interest account less Rs. 80,000 which has already been taxed in the previous year's assessment and which has therefore now been excluded cannot now be taxed because it represents payments made in years prior to the year the income of which is being assessed. Clearly however the assessee did not consider this to be a receipt of interest until he made an entry in respect of it in his interest ledger. What we are concerned with is his income of the previous year and the assessee's own view of which is his profits of the previous year as evidenced by his account books is in this case very pertinent. Assessee's argument appears to be that the money was received in a year or years prior to the previous year and should therefore be exempt from taxation. In this connection the decision of their Lordship the Judges of the Lahore High Court, dated 6th January 1926 in case No. 2 of 1925 in the application of the Delhi Cloth and General Mills Co., Limited, a copy of which is enclosed and marked A is relevant. In that case the assessee company had in the year 1918 placed towards reserve from profits a sum of Rs. 1,00,000. This sum was not taxed when assessment was made on the income of that year and in the year 1922 this amount was again brought into account and shown as profits. The assessee contended that this sum was not assessable as profits of the year 1922, in as much as these profits had accrued in the year 1918, had escaped assessment in that year and were therefore sheltered from assessment by the law of limitation. Their Lordships held that this sum was rightly taxed as profits of the year 1922 though it was received by or accrued to the company in the year 1918, primarily because the company did not treat it as profits in the former year and only treated it as such when they brought the amount into their profit and loss account. Similarly, in my view, when this assessee transfers a sum from his deposit account to his interest ledger it can rightly be treated as the profits of that year and taxed if it has not been taxed already. In my view therefore the amount legally taxable in this case in this year is the sum transferred to the interest account from the deposit account in the year 1332, less that portion of that sum which had already been taxed while still in deposit plus the interest portion of the amount actually received in that year and kept in deposit in that year.

13. In the previous year the assessee had received a sum of Rs. 25,670 from one Col. Llewelyn: This payment is apparently not a final payment and the debt has not been completely satisfied. The assessee was unable to explain to the assessing officer why he treated the whole amount realized as principal. The amount received was kept in deposit and when I was hearing the case on appeal the assessee produced a statement of this loan, which was not intelligible; I therefore asked assessee to produce a clear statement showing the amount of interest accrued on the original loan and the amount which had actually been paid and to prove that Rs. 21,000 in respect of interest from this debtor was taxed last year as claimed by the assessee. Assessee failed or refused to comply with this direction and also failed to prove that the whole of the payment represents capital as claimed. The onus was on him to prove that this payment was a payment of money which is not taxable. The assessing officer has in the absence of evidence to the contrary advanced by the assessee treated half the sum paid as payment of interest and has made assessment accordingly and the

question for decision is: "Whether the Assistant Commissioner's action in this matter is authorized by the law".

14. Assessee now alleges that this debtor has sold up all his properties and that nothing more is likely to be recovered. But this contention was advanced for the first time before me on appeal and it was not advanced before the assessing officer. Assessee had failed completely to prove that the whole or any part of this payment represents payment of capital, though the onus to do so was on him and in the circumstances I am of opinion that the assessing officer acted reasonably and to the best of his judgment in treating half the amount received as interest.

15. The assessee's method of keeping accounts of receipts of interest is as follows. He maintains a deposit register in which payments made by debtors are ordinarily first of all recorded but without any allocation between principal and interest. Subsequently if and when allocation is made an entry in respect of the interest portion of these payments is made in the interest ledger as well as in the interest account of the general ledger. This allocation is not necessarily made in the year in which the money has actually been paid to the assessee. It may be made in the following year or indeed several years later. Previous to the assessment made on the income of the year 1331, Fasli, assessee was not producing his deposit register and the income from this source on which he was being assessed was merely the amount shown as credited in the interest ledger in the previous year and this was the amount on which he claimed that he should be assessed in any year, though it may or may not have actually been received by him in the ordinary sense of the word "received" in the previous year. In connection with the assessment made on the income of the year 1331 Fasli, entries made in the deposit register were for the first time taken into account and the method adopted for the purpose of that assessment was as follows: The amounts shown in the interest ledger of that year were taken into consideration for income-tax purposes while in addition the interest portion of such deposits as were received in that year and were not allocated to interest were calculated and added to the amount shown in the interest ledger. The method followed by the assessing officer in making the assessment for the year 1332 Fasli, with which I am now dealing is as follows:—He took the amount shown in the interest ledger in the year 1332 less the portion of that amount which was taken into consideration in the previous year when he included a certain portion of the amount shown in the deposit account of 1331 Fasli as representing interest and to this he added the interest portion of the receipts of 1332 kept in the deposit account and not allocated as between principal and interest. His method of calculating what amount of any sum paid but not allocated was interest and what was principal was to take as interest that portion of the sum paid which did not exceed the total accrued interest upto date.

16. On these facts the assessee formulates the following question of law: "Whether the assessee can be precluded from raising the point that under section 3 of the Act the income received in years prior to the previous year cannot be taken into account and whether as a matter of law there can be an imaginary estoppel preventing the assessee from insisting on compliance with law by the assessing officer and whether such argument or device can be used to tax what is not taxable under the Act". This question as framed is based on the assumption that the assessing officer has not complied with the law and that something which is not taxable has been taxed by him. The question has been badly framed and in my opinion the real question which arises is as follows:—Assessee's method of accounting in respect of receipts from interest on

loans being as described above was the assessing officer's action in calculating the profits and gains of the previous year as he has done warranted by law?

17. Assessee's present contention is that by reason of the fact that the Income-tax Department is assessing to tax the amount shown in the interest ledger for the first time in 1332 though this amount was actually received by him in previous years and kept in the deposit account, we are therefore assessing him on the income of years prior to the year 1332. I do not accept this view. Assessee now claims to be assessed on what he describes as the actual receipts of the previous year, but it is perfectly clear that neither the interest ledger nor the deposit ledger shows what his actual receipts are. Further, the assessee is constantly changing his ground. At one time he contended that the sum on which he should be assessed is the sum shown in the interest ledger of the previous year, but this as explained above would include receipts in the ordinary sense of that word of years prior to the previous year. It is clear therefore that the assessee has not always interpreted in his own case the income of the previous year as meaning the same thing. Under section 13 of the Act income is to be computed in accordance with the method of accounting regularly employed by an assessee but if the method employed is such that in the opinion of the Income-tax Officer the income cannot properly be deduced therefrom then computation shall be made on such basis and in such manner as the Income-tax Officer may determine. I find that in this case the true income profits and gains of the assessee cannot be directly deduced from his account and that therefore it was incumbent upon the assessing officer to make the computation by some other method and the method which was followed is in my view the best possible method as being the one which is to the greatest possible extent based, though indirectly only on an assessee's accounts. To allow the assessee to change his ground from year to year as he is attempting to do would result in enormous sums escaping tax, while the method followed by the assessing officer in this case is in my view neither illogical, illegal nor inequitable.

18. Assessee's present contention is that income received in years prior to the previous year cannot be taken into account. As observed above the income or profits on which an assessee is taxable are the income and profits of the previous year. These are not necessarily the income and profits received in the previous year and what assessee considers to be his profits of the previous year is a relevant factor in determining what those profits are. Now, assessee has in the hearing of this application argued that the Department can do one of two things; it can tax as interest sums credited to interest in the assessee's accounts in any year whether received in that year or in a former year. Here we have assessee's own admission that it is open to the Department to tax interest actually received in a former year provided the same in question is credited to interest in the assessee's accounts in the previous year.

19. It is submitted that the question as framed should be answered in favour of the Department.

20. Difficulty has also been experienced in estimating assessee's income from the purchase of property on mortgage decrees. Assessee admitted a sum of Rs. 4,364 as receipt under this head in the previous year. Assessee keeps a suit register in which the progress of each case is supposed to be noted, but no attempt is made to keep this register upto date and in fact the sum of Rs. 4,364 referred to above is shown neither in this register nor in the interest account. On referring to the history of assessments made in previous years I find that in

the assessment made in the year 1924-25 while the assessee showed no income under this head the assessing officer estimated the income to be Rs. 6,00,000. This sum was reduced on appeal to two lacs and the order on appeal was maintained by the then Commissioner. In the assessment made in the year 1925-26, for similar reasons the assessing officer added back a sum of Rs. 3,00,000 without objection by the assessee. In that year assessee showed no income from this source in the return but admitted in the course of assessment proceedings a receipt of Rs. 20,069, to which the assessing officer added back as stated above a sum of Rs. 3,00,000 without exception on the part of the assessee. Similarly, in the year 1926-27 (the assessment with which we are now dealing), the assessee showed no income from this source in the statement filed with his return of income but subsequently admitted realisation of Rs. 4,364 only.

21. The question is: "Whether the assessing officer was right in making an estimate of Rs. 1,04,364 under this head as he has done".

22. If assessee had shown the sum of Rs. 4,364 in the suit register this might have raised some sort of presumption in his favour, but as this sum is shown neither in the interest ledger nor in the suit register, the assessing officer is in my view not acting arbitrarily and is right in concluding that assessee's income from this source is greater than that shown and in making an estimate of that income to the best of his ability. The history of past assessments shows that assessee's return of income from this source cannot be relied upon and it is for assessee to prove what his income under any head is and not for Department to do so and if the assessee fails the assessing officer must make an estimate to the best of his judgment. It is submitted therefore that this question should be answered in favour of the Department.

23. Assessee had in the previous year purchased at auction sale certain properties on which he held a mortgage and in this connection the following question of law has been formulated by the assessee: "Whether when a property is purchased in court auction by the decree holder anything is recovered except the property itself and whether under section 4 of the Act there can be a notional receipt of income from interest resulting from such a purchase which attracts the operation of section 3 of the Act and whether tax can be claimed in respect of such notional receipts".

24. As the question is one of general principle arising in every case where a decree holder buys in mortgaged property at auction sale it does not appear to be necessary to state the facts in any detail.

25. Assessee argues that when he purchases mortgaged property at auction sale this operation is a capital transaction and what he acquires is capital, but no authority has been advanced in support of this view and it is in my opinion unsound. The argument apparently is that when a creditor advances money on mortgage he acquires a contingent interest in the property mortgaged and when he subsequently buys in the property at auction sale he acquires the complete interest of the debtor in the property and this is a capital transaction. If it is true that the creditor acquired a contingent interest in the property at the time the mortgage was executed this interest is acquired for the purpose of securing the debt and for no other purpose. It is not arguable that a debt can be satisfied only by the transfer of money or cash. It can be satisfied by receipt of the money's worth and when the property finally passes to the creditor this passing of the property should be held to have satisfied the debt upto the value of the property which has passed. When a decree holder buys in mortgaged property, though the transaction is nominally a single transaction it is in reality

of a dual nature and what really happens is that the amount for which he buys in the property has been notionally received by him and with that notional receipt he purchases the property. It is submitted therefore that this question should be answered in favour of the Department.

26. The assessee had at one time advanced a sum of Rs. 32,00,000 without security to one Kumar Ganesh Singh, of a firm of brokers and the total amount of interest on this sum which had accrued up to the year of assessment was Rs. 6,09,571 in the year in question. The assessee took over from the debtor in satisfaction of this amount the following items of property movable or immovable.

	Rs.
(1) The Kajora Colliery valued at	... 7,37,339
(2) Shares in different companies valued at	.. 94,125
(3) Bills receivable by the above brokers	.. 48,809
(4) Decrees	.. 1,42,594
(5) Transfer of loan to the Agra United Company	.. 10,00,000
(6) Pronotes and handnotes	.. 52,106
(7) Hand notes from Kumar Ganesh Singh	.. 17,34,596
Total	.. 38,09,569

The argument advanced by the assessee, in this case is that, so far as regards the Kajora Colliery what has really happened is that he has purchased property to the value of that property and that this is a capital transaction and therefore the sum cannot be assessed to interest. The question at issue here is the same question as that formulated in the general question immediately above and the decision of the Court on that question will govern this point as well. I do not accept the view of the assessee that as no cash was received no sum can be held to have been realized as income, profits and gains in this transaction. In my opinion the correct way to view the transactions is to hold that the assessee has accepted in lieu of an original sum advanced without security plus interest which has accrued upto date property movable and immovable and valuable securities equal to the total amount of principal plus interest, and *prima facie* worth the valuation made by the assessee. Further in my opinion the original capital plus interest has been satisfied and an amount equal to the amount of interest which has accrued has rightly been taken as interest realised in the year. I do not think it can be contended that the satisfaction of a loan can legally be made only by the transfer of cash and it is only common sense that the transfer to a creditor of the equivalent of cash whether that be movable or immovable properly can equally satisfy a debt.

26. Assessment was made on income from this source as accruing or received in the year 1332. It appears however that all arrangements were made for the completion of this transaction and the transaction itself was completed apart from the taking over of the physical possession of the colliery in the year 1331. Assessee, on these facts, formulated the following question: "Whether if any sum is held to have been realized it was legally recovered in the year 1331 or in the year 1332". In my view the profits and gains resulting from this transaction were the profits and gains of the year 1332, for what would be the actual gains could not be ascertained, until the valuation of the colliery was finally made and accepted and possession given and this

occurred only in the year 1332. Further, this point was not taken in the grounds of appeal, was not argued before me when I heard the appeal, was not discussed in my appellate order and cannot therefore be raised at this stage in an application under section 66 (2).

27. On the expenditure side of the revenue account of this colliery for the previous year a sum of Rs. 74,982 is shown as payment of royalty. The history of this payment is as follows. According to the terms of the original lease the lessee is bound to pay a minimum royalty of Rs. 1,422 per month to the superior landlord. This was one of the terms of the original lease given by the proprietors to the original lessees. The original lessees sublet their right in the property to one Ganesh Singh and on 29th April 1925 Ganesh Singh transferred his right to the assessee on the same terms, the lessees getting a set off of Rs. 7,37,339 against his debt owed to the assessee in consideration of this transfer. The amount of royalty paid by the assessee was not for the period during which he was in possession but for the period 1st June 1922 to 31st July 1925 with interest. As assessee came into possession of the colliery on the 30th April, 1925 he was liable for royalty only for the period 30th April, 1925, to 30th September 1925, i.e., for a sum of Rs. 7,110. After the transfer of this property to the assessee he learnt of the arrears of minimum royalty still due, though in the indenture of transfer it is expressly stated that the colliery was transferred to the assessee free of encumbrances. On these facts the question for decision is—"Whether the assessee is legally entitled to deduct the arrears of royalty which had accrued in previous years up to the date of his taking possession."

28. In my view he cannot. Admittedly he is entitled to recover the excess over Rs. 7,110, being the amount of minimum royalty for the period April to September 1925, from Ganesh Singh and therefore the only legitimate expenditure on account of royalty is the proportionate amount for six months April to September 1925. Further this expense, cannot be claimed as an arrear of rent under section 10 (2) (1) of the Act, as royalty is in no sense rent. The balance may become a bad debt subsequently but that is not a question which can be discussed at this stage.

29. The assessee in a statement put in before the assessing officer had claimed a loss of roughly Rs. 78,000 in respect of the working of 2 indigo concerns of which he is proprietor. The assessing officer examined the accounts produced in support of the loss claimed only in the case of one of these factories and while he did not admit the loss he did not estimate any profits. The statement put in before him and subsequently before me did not disclose the actual profits or losses of these concerns and in particular it was impossible to ascertain the actual purchase price of indigo. At the same time as the assessee did not specifically appear to have been called on to prove the losses claimed I considered that he should be given a further opportunity of producing the accounts of these two concerns before the assessing officer. Such an opportunity was given and he appeared for the purpose before the assessing officer on the 7th and 8th of April and again on 7th of May. On these dates however there was a complete failure to explain the accounts or to show what the actual cost of indigo purchase was and finally on the 3rd day of hearing the assessee put in a petition asking that further time should be granted to enable his accountant to examine and explain the accounts. The assessing officer's report, subsequently submitted is on the record and it was open to the assessee to take a copy but he has not done so.

30. The method of financing the growing of indigo by the indigo factories is as follows:—The assessee gives out advances either to raiyats for the purpose of growing indigo or to cartmen for haulage and apart from advances the two most important items are 'Dena' and 'Pawna', Dena meaning the sum which the assessee owes to the raiyats as being the amount by which the indigo supplied by him exceeds the advance originally given for the purpose of growing indigo, while Pawna is the amount by which the value of the indigo plant supplied falls short of the original advance. If this is the system, then advances should not be taken into consideration in the profit and loss statement at all. On an examination of the accounts, however, by the assessing officer it was found that this is not the actual system employed, e.g., in checking one item he found one advance amounting to Rs. 2,988, while the raw indigo subsequently received was valued at Rs. 1,853. Pawna therefore to be paid to the factory should be Rs. 1,135 and Rs. 1,853 should be shown in the *Saltamami* account as the price of raw indigo, and Rs. 1,135 as Pawna in the Dena Pawna account. But as a matter of fact this sum of Rs. 1,135 was also included in the *Saltamami* account. Assessee's Accountant and indeed his Counsel admitted before the assessing officer that *prima facie* advances included in the *Saltamami* account had been taken twice over or that the figure showing indigo plant expenses had been so taken. It is quite obvious that it is impossible from these accounts to arrive at the actual cost of the raw indigo to the factory and in this view I am supported by the report of the Auditors, Messrs. Lovelock and Lewis, in the audit note of the accounts of the assessee's indigo concern for the year 1330, an extract from which runs as follows:—"We have not been able to verify the results of the various concerns: The figures shown in the accounts are mere receipts and payments." If it is impossible for a firm of Chartered Accountants to arrive at the net profits or loss of these concerns it is *a fortiori* impossible for this Department to do so. On this view of the case and for these reasons after considering the report submitted by the assessing officer I refused to admit any loss from these concerns in the year of assessment.

31. On these facts the question which arises for decision is:—Whether the Commissioner acting as the appellate authority can legally reject the appeal on this point without hearing the assessee on the assessing officer's report and giving the assessee an opportunity to meet the allegations made in that report. In my view he can rightly do so. The assessment was not remanded to the assessing officer and the appellate authority was still in seisin of the case and the assessing officer in making this enquiry was not acting under section 23 of the Act, but was acting under the direction specifically given by him under section 31, sub-section 2 of the Act. Sub-section 1 of section 31 deals with the hearing of the appeal, sub-section 2 directs that the Assistant Commissioner may before disposing of an appeal make such further enquiry as he thinks fit or cause further enquiry to be made by the Income-tax Officer, while sub-section 3 defines the different ways in which an appeal may be disposed of, e.g., confirmation, annulment of assessment, etc. According therefore to the natural sequence of these sub-sections this enquiry is to be made after the hearing of the appeal and before the order disposing of the appeal is passed and I can see nothing in the wording of the section to suggest that the appellate authority must give the assessee a hearing on the report submitted by the Income-tax Officer. This view is fortified by the fact that the appellate authority may himself make the enquiry as an alternative to directing the Income-tax Officer to do so. If the appellate authority adopts this course assessee will only be represented before him at the enquiry, just as they were represented in this case before the assessing officer, who made the enquiry, but he could not in that case claim a right to be heard before the ap-

pellate authority *qua* appellate authority as distinct from the appellate authority *qua* enquiring authority. I am therefore of opinion that this question should be answered in the affirmative.

32. Under section 64, sub-section 2 of the Act an assessee is ordinarily assessed by the Income-tax Officer of the area in which he resides but under section 5, sub-section 4, it is open to the Commissioner by order in writing to direct that the powers conferred on the Income-tax Officer and the Assistant Commissioner by or under this Act shall in a specified case be exercised by the Assistant Commissioner and the Commissioner, respectively and accordingly the order, a copy of which is attached and marked B* was passed by me on 25th May, 1926, authorizing the Assistant Commissioner to make this assessment and the assessment was made by the Assistant Commissioner at Patna accordingly. On these facts the following question is raised:—"Whether the assessment made by the assessing officer in this case being made at Patna and not at Darbhanga is a valid assessment".

33. In my view it is. As a result of the order passed by me under section 5, sub-section 4 referred to above, the Assistant Commissioner was vested with the powers of the Income-tax Officer of Darbhanga in respect of this specific assessment. In other words, he became for the purpose of this assessment the Income-tax Officer of Darbhanga and there is nothing in the wording of section 64 or of section 5, sub-section 4 which even suggests that in such a case the assessment must be made in the area where the assessee resides.

34. Further, the assessee did not raise this point in the petition of appeal or while arguing the case before me on appeal and he is therefore debarred from raising this question now under section 66 (2) as it does not arise out of the order on appeal. In my view therefore this question should be answered in the affirmative.

35. For the reasons given it is respectfully urged that all the above questions as formulated in this statement of the case should be decided by their Lordships in favour of the Department.

Sir S. Ahmad, L. P. Pugh, K. P. Jayaswal, Murari Prasad, S. Saran and Monohar Lal, for the Assessee.

N. N. Sarkar and C. M. Agarwala, for the Crown.

JUDGMENT.

COURTNEY TERRELL, C. J.:—In this case we have to decide certain points raised in a letter of reference, dated February 13th, 1927, by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act of 1922.

The Assessee was the late Maharajadhiraja of Darbhanga, who died on July 3rd, 1929. The Indian Income-tax Act does not contemplate assessment of the heirs of a deceased in respect of income received by him during his life time. Learned Counsel appeared before us for the heirs on behalf of whom an order for their substitution for the deceased assessee had been obtained. A preliminary question was raised by the Advocate-General as to whether, having regard to the Act the heirs were entitled to be heard. On this point it is suffi-

cient to say in the first place that this proceeding is not a suit and no question of abatement arises. We have to deal with a reference which we should have to decide, whether or not the assessee or his heirs appeared. Secondly the heirs are directly interested in the result since they are entitled to any refund of tax and even if this had been a suit and the question of parties material we would not in our discretion have decided it without hearing Counsel for the heirs; if necessary as *amici curiae*. Accordingly we have heard the arguments on behalf of the heirs.

The points raised are concerned with the income received by the assessee during the year ending in September 1925, corresponding to the Fasli year 1332.

The deceased was a nobleman of great wealth whose income was received from various sources including agricultural rent, money lending, and share dealing, and the first point concerns that part which he derived from money lending transactions. It was his custom to secure the loans by mortgages and when the debtor in any case made payment it was recorded in what has been called a "deposit" or "general" register without any allocation between principal and interest. In the ordinary course of such a business the creditor would decline to accept any instalment as being in respect of principal if any sum equal to or in excess of the instalment paid had accrued due in respect of interest, although if he chose to take a course so advantageous to the debtor he would be at liberty so to do. As against the debtor he would be entitled to appropriate any payment to the discharge of interest to the extent that it was equal to or in excess of the interest due at the date of the payment. On the other hand he might deliberately choose first to wipe off the liability of the debtor to repay the principal and thus reduce his liability to pay interest on outstanding capital, and when the capital has been so repaid only such amount as might still be outstanding in respect of interest will remain due. The question therefore of what proportion of any instalment has been received by the creditor by way of interest and what proportion by way of repayment of capital is a matter of fact in the case of each payment and depends upon the actual state of affairs as between debtor and creditor.

The assessee besides his "deposit account" kept an account which has been called an "interest" or "loan" ledger. From time to time he would make an entry in the "interest" ledger referring to the payments which had been entered in the deposit ledger, purporting by such entry to appropriate a part or the whole of such payments to the satisfaction of interest. This interest ledger, so the Commissioner finds, has not been kept up to date and in many cases accounts in the deposit ledger have been completely closed in respect of individual loan transactions and no corresponding entries are to be found in the interest ledger. Moreover, any entry in the interest ledger was not necessarily made in the same year as the receipt of and entry in the deposit ledger, of the payment to which it relates. The excuse given by the assessee for not keeping the interest entries up to date, viz., that his officials had not found time to classify how much was interest and how much was capital is manifestly absurd and was an additional and excellent reason why the Income-tax Officers should have (as they clearly did) treated his accounts with complete distrust. In the assessment made in respect of the income of the years preceding 1331 the assessee did not produce any deposit ledger. He merely produced the interest ledger and claimed to be assessed on the entries therein shown. The assessee can of course only be assessed upon interest as income, and, subject to corrections made in the *quantum* for assessment, he was so assessed. In 1332 which was concerned with the income of 1331 ending in

September 1924 the assessee for the first time produced his deposit account together with the interest account, and the Income-tax authority took the sum shown in the interest account but considered in view of the state of the accounts and other facts that it did not show what was really the sum received by way of interest. He therefore referred to the deposit account and took the whole of the payments which were entered there as having been made in the year 1331 and in the absence of any evidence of appropriation to interest, where any particular payment did not exceed the amount due in respect of interest he assumed that the ordinary course of business had been followed and added the total to the amount shown as entered in the interest ledger and assessed the assessee on the total. The assumption as to the course of business followed was reasonable and is justified by the judgment of the Privy Council delivered by Lord Buckmaster in *Venkatadadri Appa Rao v. Parthasarathi Appa Rao*(1). This method was again followed in respect of the year 1332. The methods of accounting adopted by the assessee are described in the letter of reference and one of the questions to be decided though not the first in numerical order is 'Assessee's method of accounting in respect of receipts of interest from loans being as described above, was the assessing officer's action in calculating the profit and gains of the previous year as he has done according to law?'

A great deal of argument has been addressed to us upon the difference between accounts on a cash basis and accounts on a mercantile system and the broad distinction is well understood. If the assessee had at any time presented his accounts on a mercantile basis we should have been able to survey his money lending business in respect of any year as a whole by means of a proper balance sheet and profit and loss account, but no such presentment of his business affairs has ever been attempted. Whether by design or through sheer ignorance of accounting, those who managed his affairs set forth accounts for the years in question in an almost unintelligible form in spite of every opportunity given to them by the Income-tax authorities. The accounts such as they are of the assessee whether as presented before or since the year 1331 cannot be called mercantile accounts in any sense of the word. He was at liberty, if he so chose, to prepare mercantile accounts showing the position of his money lending business as a whole from year to year. Or he could prepare a cash account of each transaction so that it could be considered separately, and the income, if any, from it might be displayed and assessed. The assessee if he adopted the latter course would be obliged to present his accounts in such a way as to show the real nature of each transaction and whether any instalment on account was received and appropriated as in respect of interest or in respect of capital. The question whether or not the accounts disclosed by the assessee do or do not disclose his true income is itself a question of fact (see *The James Cycle Co., Ltd. v. The Commissioners of Inland Revenue*(2), behind which this Court cannot go and there is a very definite finding in this case that the income cannot be deduced from the accounts disclosed. Moreover there are distinct findings supported by the assessee's own auditors that the accounts do not constitute honest disclosures of the facts.

If the assessee had been able to show that in the case of any particular instalment although it was less than the interest which had accrued due at that date yet that he had in fact been so generous to the debtor as to accept a part or the whole thereof in discharge of principal, then the officer should and

(1) I. L. R. 44, Mad. 570 at p. 573.

(2) 12 Tax Cas. 98 at p. 103.

would have omitted such part from assessment, but giving the assessee credit for common sense and business method he must in the absence of evidence to the contrary be assumed to have appropriated the whole of such an instalment to the discharge of interest. I would therefore answer the general question set forth in paragraph 16 of the letter of reference in the affirmative.

It now becomes necessary to examine particular cases and I will take first that question which is asked at the end of paragraph 9 which has reference to the case of Damodar Das. This man was in 1331 a debtor of the assessee who had some years before obtained two decrees against him in respect of principal and interest on loans. The debtor had from time to time in previous years made payments by way of instalments, and such instalments were recorded in the deposit account. But in no case was any corresponding entry made in the interest account. In 1331 the debtor had paid Rs. 38,091 and the Officer under the method described above had treated the whole of this as interest and assessed it as income. In the year 1332 the debtor paid the assessee two separate sums the one of Rs. 3,400 and the other of Rs. 2,78,000. Up to the end of this year the total amount of interest which had accrued due was Rs. 3,09,281. The assessee says that he is entitled to wait until any time he chooses before making an appropriation, and before the Officer he claimed, as to the payments made in 1332, to appropriate the earlier payment of Rs. 3,400 and a small portion, that is to say, Rs. 18,816 of the larger payment to interest, and stated that the balance of the larger payment was to be relegated to the discharge of capital. He attempts to justify this by alleging that the larger payment was the final payment to be obtained from the debtor from whom though much was still owing nothing more was to be expected and that being so he could now balance his account against Damodar Das, and that treating Rs. 2,59,184 as the capital, he was entitled to treat the whole of the previous payments including the payments of Rs. 38,091 in 1331 which had already been assessed for that year and the payments of Rs. 3,400 and Rs. 18,816 in 1332 which he admitted as assessable, as having been made in respect of interest.

Now if the creditor had really discharged the debtor by reason of the "final" payment, or if he had shown that in spite of a large balance being legally recoverable it had been necessary to close the account and the account had in fact been closed, he might reasonably have claimed to balance total receipts against capital and to be taxed on such portion received as was interest only, but in the absence of such proof the general principle must be applied and having regard to the fact that in 1331 he stated that the payment in that year was by way of interest and the payments even after those of 1332 had failed to discharge the large amount of interest due without having regard to the principal I can see no reason for holding that the payment of Rs. 2,78,000 was received otherwise than by way of interest. There is the further point that the Commissioner states in his judgment (paragraph 14) that the assessee said that the whole debt was cleared in 1333 and asked to be allowed to wait until that year would be under consideration to appropriate and classify. This further goes to show that his statement that the final payment was made in 1332 is positively erroneous. The question asked is "In the circumstances of this case what portion of the amount received from Damodar Das Burman in the previous year is legally taxable." To this I would answer that the whole payment of Rs. 2,78,000 was taxable; so that excluding the amount of Rs. 18,816 already admitted tax should be assessed on Rs. 2,71,190.

The next question is concerned with receipts from one Amar Nath Bhowe, a judgment debtor who had in previous years made payments to the assessee

on account. In the year 1332 he paid to the assessee a sum of Rs. 1,38,955. In the interest account the assessee purported to appropriate Rs. 20,000 out of this sum to interest and he also entered a sum of Rs. 1,40,107 in the interest account as having been received in years prior to the year 1332 on account of interest. Now out of this sum of Rs. 1,40,107 a sum of Rs. 80,000 had been received in the year 1331 and had already been taxed and the Department makes no claim to tax it again. But as to the balance of Rs. 60,107 the Department claims tax. The assessee contends that it was received in years prior to 1331 and contends that by reason of section 34 of the Act the claim of the Department is time barred. He says that the payments of the earlier years were expressly exempted from taxation in years prior to 1331 as not having been received on account of interest and cannot now be taxed merely because in the year 1332 they have been transferred to the interest account. An examination, however, of the final order of the Assistant Commissioner in 1330 as to the income of 1329 shows that this was not the fact. The Officer found the accounts of the assessee to be in a highly unsatisfactory condition and he did not believe in them. He scrutinised the realisations to see what was the original amount of the principal of each transaction and he assessed the assessee on an estimate of profits only, and a similar course was followed as to 1331 as to the income of 1330. The taxation was not levied on all the realisations but on such part thereof as the Officer thought should be allocated to interest and so treated as income. He took the amounts appropriated to interest in the interest account and added such amounts as had been received in the year, which, by the system I have earlier described he was entitled to consider to be interest. It is clear therefore, that the payments amounting to Rs. 60,107 have never before been appropriated to interest or taxed as income and the assessee is for the first time in 1332 making such appropriation. Following the judgment of Lord Dunedin in *Commissioners of Taxes v. The Melbourne Trust Limited*(1) they must be treated as income received in the year of appropriation. Never having been treated as non-taxable and excluded, they are not time barred. The question is "What is the amount of profits and gains arising out of the payments made by this judgment-debtor legally taxable in this year?" I would answer that the sum of Rs. 60,107 is so taxable.

The next question relates to a payment of Rs. 25,670 from a Col. Lewellyn entered in the deposit account. The assessee asserted at the hearing on appeal before the District Commissioner acting as Assistant Commissioner and not until then, that this was a final payment and was appropriated to the capital of the loan. He could not produce any intelligible statement of the loan transaction or of the payments which had preceded the one in question. Before this Court his learned Counsel could offer no better account. The Assistant Commissioner treated the payment as income and assessable. The question propounded is "Whether the Assistant Commissioner's action in this matter is authorised by law". The contention to the contrary is practically unarguable and the answer should be in the affirmative.

The next question is concerned with the return made by the assessee of income derived from the purchase of mortgaged properties under mortgage decree sales. The assessee admitted a receipt of Rs. 4,364 under this head in the previous year. The assessee had a suit register but made no attempt to keep it up to date. In respect of the year 1330 the assessee showed no income under this head. The Officer assessed him at six lakhs which sum was reduced to two lakhs on appeal. In respect of the year 1331 he admitted a receipt of Rs. 20,069 to which the Officer added three lakhs and the assessee did not

appeal, and in respect of the year under assessment the Officer on appeal has added one lakh to the assessee's return. The question is "Whether the assessing Officer was right in making an estimate of Rs. 1,04,364 under this head as he has done". It is the duty of an assessee to keep and present his accounts to show the actual income made by him. If he fails to do this he must put up with the estimate by the officer made to the best of his ability. The case of *Raja Raghunandan Prasad Singh v. Commissioner of Income-tax*(1) recently decided by a full bench of this Court settled finally the question of principle and the only point here is one of *quantum*. Learned Counsel for the assessee has argued that the Officer is not entitled to make a guess without evidence, and I agree with that contention, but in this case the state of affairs in the previous years coupled with the fact that the assessee had a large mortgage loan business and must have enforced mortgages by sale on many occasions afford ample material for the assessment made. I would answer the question in the affirmative.

The next question is concerned with a transaction between the assessee and one Ganesh Singh. According to the finding Ganesh Singh the debtor in 1332 owed the assessee a sum of 32 lakhs as principal and Rs. 6,09,571 as interest in respect of a loan without security. In that year the assessee and the debtor made a fresh arrangement to deal with the outstanding debt. The assessee took over a colliery, shares, bills receivable by the debtor, the benefit of a decree, a transfer of a loan to a company and handnotes from third parties at a valuation in respect of each item so taken over. This cleared off Rs. 20,74,973 and the debtor executed fresh handnotes in respect of the balance of Rs. 17,34,596. The Department contends that this transaction discharged the liability for capital and interest of the loan and that the assessee is liable to assessment on the amount of the interest which must be taken to have been received when the conveyance was executed (as it was) in 1332.

But in every case the real nature of the transaction must be looked at and in my opinion this transaction was in effect and substance the acceptance of a proposal by the debtor which might be expressed in these words; "As to this amount of Rs. 38,09,569 which I owe you, I will hand over to you a quantity of valuable property which shall discharge the liability to the amount which it may in fact be worth, and as to the balance I shall have to continue to owe it, but in order to record the amount still due I will execute fresh handnotes to the amount of that balance." The assessee contends that the transaction cannot be considered closed until the balance of liability represented by these notes has been realised or written off as a bad debt.

Now it is true that a debt may be discharged by consideration other than cash, and that in taking account of profit and loss on a loan liability discharged by such consideration the true value of the consideration must be taken into account. It is also true that a handnote is in itself a valuable security capable of valuation and not differing in this respect from a colliery or shares. Further it is quite possible that the assessee might be unable in law to sue on the old debt but might be forced after the transaction to rely upon his new handnotes. But none of these propositions of law alters the real nature of the transaction which in my opinion is, on the facts found, as I have described. If the debtor had not executed the handnotes, the assessee if he accepted the other items of consideration could only have sued the debtor for the balance. The real nature of the transaction, which is the test to be applied, is not affected

by the fact that the assessee was given an additional weapon in the form of the handnotes for the recovery of the balance from the debtor. The case of *Raja Raghunandan Prasad Singh v. Commissioner of Income-tax*(1) was decided for reasons which have no bearing here and I do not think that it helps the assessee. In my opinion his real strength lies in relying upon the Court to ascertain the real nature of the transaction however it may have been concealed by the method of book-keeping. This is not a matter of the distinction between the mercantile and the cash systems of book-keeping. Throughout, the money lending affairs of the assessee have been recorded and treated on a system which is *sui generis*. The case of *Raja Raghunandan Prasad Singh* proceeded upon the cash basis strictly so called and it has no application one way or the other. The question is not formally put in the letter of reference, but for the sake of convenience may be answered, whether the interest can be considered to have been received and assessable, and in my opinion such question must be answered in the negative. If, on the other hand, I am wrong about this there is the further question whether the income was received in 1331 or 1332. It is conceded on both sides on April 29th, 1925, that is in 1332, that the title to the assets conveyed passed on that date. Had the amount of interest been assessable it would have been assessable in respect of 1332.

The next point is concerned with a claim by the assessee to make a certain deduction of Rs. 74,982 in respect of the revenue account of the Kakora colliery. This colliery was one of the assets taken over in discharge of Ganesh Singh's liability but it has here to be considered under another aspect. The original lessees from the owner of the colliery sublet their right to Ganesh Singh and by the instrument of transfer dated the 29th April 1925, Ganesh Singh transferred his right to the assessee on the same terms. Under the terms of the original lease the lessee is bound to pay a minimum royalty of Rs. 1,422 a month to the landlord. When the assessee came into possession of the colliery he found that certain arrears of the minimum royalty were still due in respect of the tenancy prior to the date when he took it over, although the transfer had expressly stated that the colliery was transferred to the assessee free of incumbrances. In order to be able to carry on the colliery the assessee in 1332 paid up the arrears amounting to Rs. 67,872 the liability to pay having been incurred before 1332 the year of assessment. The question for decision is "Whether the assessee is legally entitled to deduct the arrears of royalty which had accrued in previous years up to the date of his taking possession."

Now it is true that in some cases the royalty based upon the amount of mineral raised may be treated as a capital expenditure, that is to say, as part of the purchase price for the mineral. On the other hand this royalty is a minimum royalty, that is to say, the tenant has to pay it whether or not he raises any coal at all, and moreover if the assessee fails in any year to extract sufficient coal to enable the royalty to be paid upon the amount so raised he will have an opportunity in later years to recover that coal which will have remained under the ground and thereupon will have to pay royalty which will be liable to tax. It has been decided [See *Manindra Chandra Nandi v. Secretary of State for India*(2), and *In re: Raja Jyoti Prasad Singh Deo*(3)] that a receiver of royalty is assessable, therein following Lord Blackburn's decision in *Coultness v. Black*(4) that a royalty may properly be considered as rent. It is further to be noticed that since the previous tenants have not paid

(1) 4 I. T. C. 123.

(2) I. L. R. 34 Cal. 257.

(3) 1 I. T. C. 103.

(4) 1 Tax Cas. 287; 6 A. C. 315 at p. 335.

the rent for the period of the arrears they have not been able to make a deduction in their account under the expenses heading for that period. In addition to the contention that the royalty should be considered as capital expenditure and not as rent the Department urge that inasmuch as the rent accrued due in the years prior to 1332 it cannot be considered as having been paid in that year. Furthermore it is argued that it is open to the assessee to recover the amount of the arrears paid by him from his transferor, Ganesh Singh. But having regard to the normal course of business in mining leases it may be assumed that the rent was not a mere personal liability but that the strict fulfilment of the obligation to pay the minimum was a condition without which further mining operations could not be effected. Moreover although the rent cannot properly be deducted until it has in fact been paid I see no reason why if paid in arrears it should not be deducted as though it had accrued in the year in which it was paid. It was a liability in the nature of a charge in the year 1332 and in that year it was paid. I would therefore answer the question in the affirmative.

The next point for consideration is concerned with the claim by the assessee to the benefit of an alleged loss of Rs. 78,000 in respect of the working of two indigo concerns. To establish this loss certain accounts were put in before the assessing Officer which were held by him to be unintelligible, and he held that no such loss was established. On appeal before the Commissioner the assessee contended that the accounts put in by him did in fact establish a loss. The Commissioner sent back the case for a further report and for the assessee to have an opportunity of producing the detailed accounts, with a view if possible to establish the loss which he persistently alleged. The assessee asked that when the assessing Officer's report should be forthcoming that he might be heard upon it. When, however, the Commissioner received the assessing Officer's report he made his decision without a further hearing of the assessee. The assessee complains that in so doing the Commissioner was breaking a well-known rule of natural justice that a party should not have a decision against him upon materials upon which he has had no opportunity of addressing the tribunal. The only point for consideration therefore is whether the assessing Officer's report contained any new material and an examination of that report shews very conclusively that such further materials, if any, as had been put before the assessing Officer had entirely failed to shake him in his original view that the accounts were unintelligible and did not disclose the alleged loss. The assessing Officer was fortified in his original view by the report of the auditors employed by the assessee to investigate the accounts of the two concerns in which they say "We have not been able to verify the results of various concerns; the figures shewn in the accounts are mere receipts and payments". The report therefore is of a negative and not an affirmative character and contains nothing new. The real object of the assessee was frankly admitted before us by learned Counsel on his behalf who stated that he wished to go behind the report and to show that if the very voluminous so-called accounts were properly examined with the aid of further skilled assistance which was not before the assessing Officer the assessing Officer might have come to a different conclusion. In order, however, to take advantage of the general principle and to show that he has been denied natural justice the assessee must establish that the report itself contained new material and this he has signally failed to do. The question is put as follows:—"Whether the Commissioner acting as the appellate authority can legally reject the appeal on this point without hearing the assessee on the assessing Officer's report and giving the assessee an opportunity to meet the allegations made in that report." Having regard to the nature of the report in this case the Commissioner was, in my opinion, right in the course taken by him.

A final question arose on the matter of jurisdiction. The assessee argues under section 64 sub-section (2) of the Act that the assessment order must be made in Darbhanga, that is to say, in the area where the assessee is ordinarily assessed by the Income-tax Officer but under section 5 sub-section (4) the Commissioner directed that the powers conferred on the Income-tax Officer were to be exercised by the Assistant Commissioner. The actual hearing took place at Patna with the consent of the assessee and the only point in the assessee's objection is that the signature of the Assistant Commissioner was actually appended not in Darbhanga but in Patna. This point was not raised in the petition of appeal to the Commissioner or while arguing the case on appeal. It is of no merit and has no substance and the question "Whether the assessment made by the assessing Officer in this case being made at Patna and not at Darbhanga is a valid assessment" should be answered in the affirmative.

DAS, J.:—I entirely agree. I propose to deal with two of the points which have been argued before us, one on behalf of the Crown by the Advocate General, the other on behalf of the assessee by Mr. Pugh. The point made on behalf of the Crown is that, the assessee being dead, the proceedings have abated and that nothing more can be done. The Advocate General was aware of the decision of Sankey J. (as he then was) in *Smith v. Williams*(1) to the effect that where the proceedings have once commenced, they must go forward until adjudicated upon, notwithstanding the death of the assessee after the commencement of the proceedings, and that if there be no procedure entitling the legal representative of the assessee to continue the proceedings, the Court will mould a convenient form of procedure to meet the case. The Advocate General however, contended that the English Statute is so radically different from the Indian Statute in regard to the rights and liabilities of the legal representative of the assessee that it is impossible that the decision in *Smith v. Williams*(1) can apply to the facts of this case.

Now it does appear that whereas in England the Crown is at liberty to proceed against the estate of the assessee in the event of the assessee dying before the assessment is complete, there is no provision in the Indian Statute for the assessment to income-tax of the estate of a deceased person. But does it follow that the case before us does not attract the operation of the rule which was so carefully formulated in the case to which I have referred? I think not; for the decision in the English case rests on the principle that it is not possible to apply the common law doctrine of abatement to proceedings of this nature, since the whole of the procedure connected with the income-tax matters is the creature of Statute, and not on the principle that, as there is power to proceed against the estate of the deceased assessee in the matter of assessment, so there must be power to continue proceedings of this nature against such estate. The case was not argued from this footing and was not decided on this footing. It was decided on the footing, as I have just said, that there is no abatement in these proceedings, and that if there is, the proceedings are not dead, but are suspended only and are capable of being revived; and that where the apt procedure is not provided by the statute, the judge must himself mould a convenient form of procedure to give effect to the manifest intention of the Legislature that there should be a hearing of, and an adjudication upon, every case started in this way.

This being the position, the English case will have direct application if it is clear that the Indian Statute contemplates a final adjudication upon a case stated under section 66. In my judgment, there is no doubt that it does.

Paragraph (1) gives liberty to the Commissioner to draw up a statement of the case and refer it with his own opinion thereon to the High Court, either on his own motion, or on reference from any income-tax authority subordinate to him if a question of law arises in the course of any assessment. Paragraph (2) confers a power on the assessee to require the Commissioner to refer to the High Court any question of law arising out of an order under section 31 or section 32, provided he satisfied certain conditions clearly specified, and it provides that "the Commissioner shall.....draw up a statement of the case and refer it with his own opinion thereon to the High Court." Paragraph (3) gives the assessee liberty to apply to the High Court, if the Commissioner refuses to state the case on the ground that no question of law arises, and it provides that "the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and the Commissioner shall state and refer the case accordingly." So far the Legislature has been at pains to make it clear that both the assessee and the income-tax authority have the right to have a question of law arising out of an assessment decided by the High Court. Paragraph (5) clearly provides for a hearing of, and an adjudication upon, the case as stated by the Commissioner, and it directs the High Court to send to the Commissioner a copy of its judgment, and it provides in distinct terms, "the Commissioner shall dispose of the case accordingly." The proviso to paragraph (7) enacts that "if the amount of an assessment is reduced as a result of such reference, the amount overpaid shall be refunded with such interest as the Commissioner may allow". In my judgment the Legislature has said very distinctly that once a reference has been made under paragraph (1) or an application has been made either under paragraph (2) or paragraph (3) the proceedings have commenced, and that once the proceedings have commenced they must go forward until a final decision is reached by the High Court, provided that there is a question of law arising out of the assessment. If this be the position, (as, I think, it is) then the English case to which I have referred has direct application, and I must hold that we are bound to adjudicate upon the case as stated by the Commissioner, notwithstanding the fact that the assessee is now dead.

The other question arises with reference to a loan of Rs. 32,000,000 advanced by the assessee to Kumar Ganesh Singh. The Income-tax Officer assessed the assessee on the sum of Rs. 6,09,571 said to be the interest realised by the assessee from Ganesh Singh during "the previous year". I take from the statement of the case as to what actually happened: "In the year in question the assessee took over from the debtor in satisfaction of this amount", that is to say, the amount advanced together with the accrued interest thereon, the following items of property movable or immovable.

	Rs.
(1) The Kajora Colliery valued at	7,37,339
(2) Shares in different companies valued at	94,125
(3) Bills receivable by the above brokers	48,809
(4) Decree	1,42,594
(5) Transfer of loan to the Agra United Company	10,00,000
(6) Pronotes and handnotes	52,106
(7) Handnotes from Kumar Ganesh Singh	17,34,596
Total ..	38,09,569

It will be noticed that the assessee took properties of the value of Rs. 20,74,973 and the promise of the debtor to pay him on demand the sum of Rs. 17,34,596 in satisfaction of his claim for Rs. 38,09,571. The question which arises on these facts is, can it be said that the assessee has earned a profit of Rs. 6,09,571 since it is clear that the assessee has not actually realised that sum, either actually or notionally? The view of the Department has been very clearly put in the order of the Commissioner dated the 24th May 1927. "In my opinion," says the Commissioner, "the correct way to view the transaction is that the assessee has accepted in lieu of an original sum advanced without security plus interest which has accrued up to date property movable and immovable and valuable securities equal to the total amount of principal plus interest and *prima facie* worth the valuation made by the assessee. Therefore, in my view, the original capital plus interest has been satisfied, and an amount equal to the amount of interest which has accrued has rightly been taken as interest realised in the year."

Now we are not concerned with what the position may be as between the debtor and the creditor. The sole question from the point of view of the income-tax administration is, can it be said that an income of Rs. 6,09,571 has accrued or has arisen or has been received so as to attract the operation of the Income-tax Act. We know that there must be an incoming to satisfy the test of income. That "incoming" may be actual, as when the sums are actually realised and go to swell the assets of the assessee, or it may be notional, as when the sums are not actually realised but are treated in the accounts as having been realised. It is not suggested in this case that the accounts show the realisation of this sum of money by the assessee. In order to succeed, then, the Crown must establish that the sum of Rs. 6,09,571 was actually received by the assessee.

The Advocate General puts his point thus: It is not necessary, so he argues, that actual money should be received to satisfy the test of income. It is sufficient, he contends, that the assessee has received either money or money's worth. He might have taken a picture, a plate or a piece of jewellery, in full satisfaction of his claim; and it can make no difference according to the argument of the Advocate General, that instead of taking a picture, a plate or a piece of jewellery, the assessee has chosen to take a promissory note from his debtor. The answer to the argument is that, once the creditor has accepted a picture, a plate or a piece of jewellery from the debtor, the liability of the debtor is at an end; and the article which the creditor has taken from the debtor represents, according to the valuation put upon it by the former, the entire sum of money due to him. But when a creditor has taken a promissory note from a debtor the consideration being a sum of money already due to him, the liability of the latter is not necessarily at an end, and it is open to the creditor under certain circumstances to sue for the original consideration. "When a cause of action for money is once complete in itself, whether for goods sold, or for money lent, or for any other claim, and the debtor then gives a bill or note to the creditor for payment of the money at a future time, the creditor, if the bill or note is not paid at maturity, may always, as a rule, sue for the original consideration, provided that he has not endorsed or lost or parted with the bill or note, under such circumstances as to make the debtor liable upon it to some third person." *Sheikh Akbar v. Sheikh Khan* (1). I have no doubt whatever that the taking of a promissory note in consideration of a debt already due is not the same

thing as the taking of a picture, a plate, or a piece of jewellery in satisfaction of one's claim. In the latter case the liability is extinguished; in the former case the liability remains.

It was then urged that the promissory note executed by Ganesh Singh is a negotiable instrument and therefore a valuable security; and that, as it must be deemed to have some value, it was clearly the duty of the assessee to value it before the Income-tax Officer; and that, as he failed to do so, he must now be bound by the value put on it by the Income-tax Officer. If I am right in taking the view that the execution of the promissory note did not extinguish the liability of Ganesh Singh on the original consideration, then this question does not arise; for the liability still remaining, the promissory note clearly does not operate as a payment. Two cases have been referred to and it is right that I should deal with them.

In *Californian Copper Syndicate v. Harris*(1), the facts were these: The appellant company was formed, as it appeared to the Commissioner, with a view to resell the property acquired by it. It resold a property that had been acquired and worked by it at a profit; the purchase money being received by it, not in cash, but in fully paid up shares of the company buying the property. The main question canvassed in the case was whether the transaction did not amount to a substitution of one form of investment for another so as to take the case out of the Income-tax Act. We are not concerned with that aspect of the case. But it appears to have been also argued that, as actual cash was not received, there was no profit in the contemplation of the law which could be assessed to income-tax. In dealing with this point, Lord Trayner said as follows: "But it was said that the profit—if it was profit—was not realised profit, and, therefore, not taxable. I think the profit was realised. A profit is realised when the seller gets the price he has bargained for. No doubt here the price took the form of fully paid shares in another company, but if there can be no realised profit, except when that is paid in cash, the shares were realisable and could have been turned into cash, if the Appellants had been pleased to do so. I cannot think that income-tax is due or not according to the manner in which the person making the profit pleases to deal with it. Suppose, for example, a seller made a profit on a trade transaction, but leaves the price (including the profit) in the hands of the buyer at so much per cent, interest. That he so deals with it, rather than take the cash into his own pocket, would not affect the claim of the Revenue for the tax payable on the profit. No more, in my opinion, does it affect the liability for the tax that the Appellants left their profit in the hands of the company they sold to and took the company's shares as their voucher". It will be noticed that the case was one of sale, the price being received by the vendor company, not in cash, but in fully paid up shares, which, as Lord Trayner was careful to point out "were realisable and could have been turned into cash."

The first answer to the arguments founded on this case is that there was no doubt whatever, in the case cited, that the liability of the purchaser company was at an end, once they paid the price in fully paid up shares, so that it followed that consideration was received by the vendor company. In the present case, the liability of the debtor was not at an end, so that it could not be said that the payment was made. The second answer is that although there is a recognised market for purchase and sale of shares, so that "the shares were realizable and could have been turned into cash", I know of no market in Darbhanga where promissory notes can be bought and sold. The Advocate General rather insisted that there is one passage in the judgment just cited which

exactly applies to the facts of this case, the passage in which the learned Judge suggests that if a seller made a profit on a trade transaction, but left the price (including the profit) in the hands of the buyer at so much per cent, interest, the profit made but not actually received is assessable to income-tax. For myself I would always resist every attempt that may be made to isolate passages from the judgments of eminent Judges, take them out of their setting, and to apply them to case arising under wholly different circumstances. I have no difficulty whatever in understanding the passage if read with the context which shows that, in that case, the profit had actually been earned and received, not, it is true, in cash, but in shares "which were realisable and could have been turned into cash"; but I suggest with great respect, that it has no application to a case where the profits have not been realised and the old liability has not been extinguished.

The decision in the other case relied upon, *The Scottish and Canadian General Investment Company, Limited v. A. Eassen* (1) is to the same effect and does not materially advance the case of the Crown. The appellant company held certain 5 per cent. mortgage bonds of the Western Canada Power Company, Limited. The latter company was unable to meet the coupons which fell due for payment on the 1st January 1916 in respect of the interest on the bonds for the half year from 1st July 1915. A reorganisation of the finance of the debtor company took place which involved the formation of a new company. The appellant company surrendered its holding of bonds of the old company, with the unpaid coupons attached, and received in exchange 5 per cent bonds of the new company of equivalent face value bearing interest from 1st July 1917, together with an issue of ten year 7 per cent debentures of the new company, equal in face value to 10 per cent of the face value of the surrendered bonds. It was held by the Lord President that the face value of the ten year 7 per cent debentures was the precise equivalent of the two years interest at 5 per cent on the original holding of bonds for the two years which elapsed between 1st July 1915 and 1st July 1917. This being the position the only question was whether income-tax could be levied on those debentures. It was held that income-tax could be levied, for though the interest was not received 'in cash,' "the debentures themselves were saleable and had a value on the market". As the Lord President pointed out, "The question is just one of ascertaining the profits and gains of the company, and if, instead of receiving cash, the company get a saleable security, that saleable security is just part and parcel of the company's profits and gains". The principle established in the case is clear enough; but, in my judgment, it has no application here, since it has not been established that the promissory notes in question have "a value on the market". I therefore agree that the question with reference to the transaction with Ganesh Singh should be answered in favour of the assessee.

With regard to the other questions argued before us I entirely agree with the judgment of my Lord, and have nothing further to add.

KULWANT SAHAY, J.:—This is a reference under section 66(2) of the Indian Income-tax Act (1922). The assessment relates to the income of the assessee in the Fasli year 1332, ending in September 1925. The tax levied on account of income-tax and super-tax is Rs. 13,25,987-5-0 on an assessed income of Rs. 33,37,204.

The objections of the assessee relate to matters which may be classified under eight heads; viz., (1) income derived on the foot of two decrees passed in favour of the assessee against one Damodar Das Barman; (2) income derived

on account of realisation of the debt due from one Amar Nath Bose; (3) income derived from a debt due from one Col. Lewellyn; (4) income derived from mortgage execution sales; (5) income derived from the transaction with one Kumar Ganesh Singh; (6) income derived from the Kajora Colliery; (7) losses incurred by the assessee in certain indigo concern; and lastly a point is raised as regards the jurisdiction of the Income-tax Officer to make the assessment.

In order to understand the nature of some of the objections it is necessary to set out the system of accounting adopted by the assessee. It appears that the assessee keeps a register known as the deposit-register in which he enters all sums received from his debtors without any specification as to whether the sums received were on account of principal or interest. He also keeps an account known as the loan account. In this account he transfers from time to time sums entered in the deposit register which he appropriates on account of interest on the debts received by him. It has been found by the Commissioner that the interest account is not kept up to date and the entries in the interest account are not necessarily made in the year in which the money has actually been received by the assessee, having found as a fact that in several cases although the account had been closed in respect of particular transactions no entries have yet been made in the interest account.

The assessee did not produce his deposit-register when assessments were made by the Income-tax Department for the income of the years previous to the income of the year 1331 Fasli. On those occasions he merely produced his interest account and the Income-Tax Department assessed his income on the basis of the entries made in the interest account. He produced his deposit-register for the first time when assessment was made on the income of the year 1331 Fasli. On this occasion the Income-tax Officer found on examining the books that huge sums of money entered in the deposit-register had not been transferred to the interest account. He had to find out what was the interest on the loans actually realised by the assessee in the year 1331 Fasli. He could not rely upon the entries made in the interest account and he had to find out the actual amount realised on account of interest in the year under consideration. He found that large sums had been kept in the suspense account to the detriment of revenue. He, therefore, in that year found to the best of his ability what ought to be considered to be receipt on account of interest and he accordingly made his assessment on the sums which he considered ought to be taken as received on account of interest. In the year under consideration in the present reference the assessee produced his deposit register as well as his loan-register in which the interests were entered.

The system of accounting kept by the assessee was not the cash system as it is generally known: it was a peculiar system in which the actual realizations in the year were noted and the sums received were kept in suspense for a number of years. The Income-tax Department was bound under section 13 of the Act to compute the income, profits and gains of the assessee in accordance with the method of accounting regularly employed by the assessee, but if the method employed is such that in the opinion of the Income-tax Officer the income, profits and gains can not properly be deduced therefrom the law authorises him to make a computation upon such basis and in such manner as the Income-tax Officer may determine. In the present case, having regard to the findings arrived at by the Commissioner, the Income-tax Officer was justified in adopting the method that he did in order to find out the actual income, profits and gain of the assessee on account of money-lending business.

As regards the first item, viz., the debt due from Damodar Das the facts found are these: A large sum of money was due from Damodar Das on the foot of two decrees and Damodar Das had been making payments to the assessee over a number of years. All these payments were entered by the assessee in the deposit-register and nothing had been transferred to the interest account. In the year 1332 two sums of Rs. 3,400 and Rs. 2,78,000 were paid by Damodar Das to the assessee. The assessee wants to treat the first payment of Rs. 3,400 as interest and out of the second sum of Rs. 2,78,000 he claims that only Rs. 18,816 was on account of interest and the balance on account of the capital. The Commissioner has found that the total amount of interest which has accrued to the assessee on account of this debt up to the end of the year 1332 is Rs. 3,09,281. Out of this sum only Rs. 38,091 which was the amount received in the year 1331, was assessed to income-tax in that year. The Income-tax Officer has given a credit for this sum of Rs. 38,091 and has held that as the payment in the year 1332 exceeded the balance of the total interest tax should be assessed upon the whole of the balance of the interest. The question is whether the Income-tax Officer was justified in doing so. The objection on the part of the assessee is that by adopting the method which has been adopted by the Income-tax Department they have assessed tax on the income received not only in the 'previous year' but also in the years prior to that. Having regard to the facts found, I am of opinion that the Income-tax Officer was justified in assessing tax upon the entire amount of interest found due. It is clear from the method of accounting adopted by the assessee that no appropriation was made by the assessee on account of interest in the previous years, and the whole of the amount received was kept by him in suspense account. A creditor is entitled to keep the amounts received by him from his debtor in suspense and in case the creditor *bona fide* keeps the amount in suspense he is entitled to say that he is not liable to assessment so long as the appropriation has not been made and the account has not been settled; but if it is found that the suspense account is not kept *bona-fide* the Income-tax Department would be entitled to find for themselves what was the amount received on account of interest. I am of opinion that the method adopted by the Income-tax Officer was correct and the assessment on this head was according to law.

The second item is the transaction with one Amar Nath Bose. It appears that in 1332 Fasli he made a payment to the assessee of the sum of Rs. 1,38,955. Out of this sum the assessee in that year transferred a sum of Rs. 20,000 to the interest account and the balance was kept in the deposit account. In the interest account of this year the total amount shown against this debtor is Rs. 1,60,107 made up of the sum of Rs. 20,000 which he had transferred to the interest account in 1332 out of the payment of Rs. 1,38,995, and of Rs. 1,40,107 which represented a transfer from the deposit account of the years prior to 1332. The Income-tax Officer has charged to tax in the year 1332 the entire amount of Rs. 1,60,107 less a sum of Rs. 80,000 which was taxed in the preceding year 1331. The question propounded is: What is the amount of profits and gain arising out of the payments made by this judgment debtor legally taxable in this year? The objection of the assessee is that the sum of Rs. 1,40,107 cannot be taxed in the year under consideration inasmuch as this was a payment in the years prior to 1332. He contends that the Income-tax Officer in making the assessment over the income of the year 1331 had assessed tax only upon the sum of Rs. 80,000 and by doing so had exempted the balance from tax and, as the balance had thus escaped taxation, it could not be taxed in the year under consideration. Now, it is clear that having regard to the method adopted in making the assessment on the income of the year 1331 there was no exclusion of any amount received as interest. In that year the Income-tax Officer pro-

ceeded on the actual receipt of the year 1331. He did not come to any finding as regards the income received in the years prior to 1331. When the interest account was produced before the Income-tax Officer during the present assessment it was discovered that the sum of Rs. 1,40,107 was appropriated by the assessee on account of interest in that year. The reason why this sum was shown in the interest account of this year appears to be that the assessee wanted to change his system of accounting from the cash system into the mercantile system. He made an application to the Income-tax Officer to allow him to change his system of accounting. The Income-tax Officer very properly stated that he wanted to satisfy himself that by this change of system there would be no detriment to the revenue. After certain proceedings the assessee withdrew his application to change his system of accounting, but he had already made entries in the interest account on the mercantile system and this showed the sum of Rs. 1,40,107 as interest realised by him on account of the debt in question. It is clear having regard to the facts found that there was no exclusion by the Income-tax Officer of any sum in the assessment for the income of the year 1331 and that, therefore, the Income-tax Officer was justified in taking into account the sum of Rs. 1,40,107 on account of interest in making the assessment of the transaction in question; and the assessment is legal and justifiable.

The third item relates to a sum of Rs. 12,835 out of a sum of Rs. 25,670 received by the assessee from Col. Lewellyn. The assessee wanted to treat the whole of this amount as realization of principal and therefore exempt from taxation. The Income-tax Officer has taken half of this sum as representing interest. The question is whether he was justified in doing so. The learned Commissioner is of opinion that as the assessee had completely failed to prove that the whole or any part of the payment represented payment of capital, and the onus thereof was upon him, the assessing officer acted reasonably and to the best of his judgment in treating half the amount received as interest. I am of opinion that the view taken by the Commissioner is correct.

The fourth item relates to mortgage execution sales. It appears that the assessee sometimes purchased properties in execution of mortgage decrees. In the year under consideration the assessee admitted the sum of Rs. 4,364 as receipt under this head. The Income-tax Officer was not satisfied that this was the only sum received by him in the year under assessment and he added a sum of Rs. 1,00,000 to this sum and assessed the tax upon the sum of Rs. 1,04,364. Having regard to the facts set out by the Commissioner the Income-tax Officer appears to be justified in doing so. It is contended that this is a pure guess not based upon any evidence, and the Income-tax Officer was bound to proceed upon some evidence in making the assessment. No doubt it is a guess; but under the circumstances set out in the referring order of the Commissioner I am of opinion that it was for the Income-tax Officer to make the assessment to the best of his ability and it is not open to us upon this reference to say that he was not justified in doing so.

The fifth item is the transaction of Kumar Ganesh Singh. Kumar Ganesh Singh was a member of a firm of brokers and it appears that a sum of Rs. 32,00,000 was due to the assessee from him for which there was no security. Kumar Ganesh Singh appears to have settled his account with the assessee in this way—he transferred to the assessee a colliery, shares in different companies, bills receivable by him, decrees held by him against third persons, loans due to him from third persons, all of which were valued at a sum of Rs. 20,00,000 and odd. For the balance of the amount due from him on account of principal and

interest, which latter sum was calculated at Rs. 6,09,571 Kumar Ganesh Singh gave handnotes to the assessee for the sum of Rs. 17,34,596. The total of the valuations of the colliery, of the shares, of the bills, etc., transferred to the assessee and the sum of Rs. 17,34,596 for which handnotes were given, came to Rs. 38,09,569. The Income-tax Officer treated the whole of this sum as payment by Kumar Ganesh Singh to the assessee. He, therefore, assessed tax upon the sum of Rs. 6,09,571 which was the amount of interest found to be payable by Kumar Ganesh Singh to the assessee. The question is whether this was justifiable under the law. The objection of the assessee is that this was not an income which accrued to him within the meaning of the law upon which tax could be assessed. It is argued on behalf of the Department that, although the payment was not in cash, it was a payment of money's worth and the Department was therefore justified in assessing the amount to tax. On behalf of the assessee reference was made in this connection to the decision of this Court in *Raja Raghunandan Prasad Singh v. The Commissioner of Income-tax*(1) known as the Monghyr case. In that case it was held that interest on a mortgage cannot be said to accrue to the assessee as it falls due every year but it accrued within the meaning of section 4 of the Income-tax Act when it is actually received and that the words "income arising or accruing" are not equivalent to the words "debts arising or accruing" as to give them that meaning is to ignore the word "income" and there must be a "coming in" to specify the word income, and reliance was placed upon the decision in *St. Lucia Usines and Estates Company, Ltd., v. Colonial Treasurer of St. Lucia*(2).

Having regard to the true nature of the transaction I am of opinion that the Income-tax Department was not justified in assessing tax upon this transaction. The transaction was merely a substitution of one debt for another and there was no accrual of income in order to justify an assessment to tax. On examining the true nature of the transaction I find that no income accrued to the assessee which is liable to taxation. I am aware that income need not necessarily be an income of cash but it may be in the nature of something other than cash; but in the present case there was no income as the sum of Rs. 17,00,000 and odd for which the handnotes were given were only an acknowledgement of a previous debt and not actual payment to the assessee. A further question is raised under this head as to whether the income, if any, was liable to assessment in the year 1332 or in the previous year. Having regard to the facts found by the Commissioner, I am inclined to hold that the income, if it accrued at all, accrued in the year 1332 and would be liable to assessment if it was treated as an income under the law.

As regards the sixth item, it appears that a colliery known as the Kajora Colliery was transferred by Kumar Ganesh Singh to the assessee in settlement of his debt. The colliery was demised under a lease under which the lessee was bound to pay a minimum royalty of Rs. 1,422 per month to the superior landlord. In making the transfer to the assessee Kumar Ganesh Singh had represented that there were no arrears due and that the colliery was free from encumbrance. In going to take possession, however, the assessee discovered that a sum of Rs. 74,982 was due to the superior landlord on account of minimum royalty for the period prior to his taking possession of the colliery and he paid this sum to the superior landlord. The question is whether he is entitled to claim deduction for this payment. The Commissioner has found that the minimum royalty is an allowable deduction but the sum paid by the assessee on account of the arrears of the minimum royalty cannot be deducted as

(1) 4 I. T. C. 123.

(2) (1924) A. C. 508.

under the terms of the transfer the assessee would be entitled to recover the sum from Kumar Ganesh Singh. I am of opinion that the sum paid by the assessee on account of the arrears of royalty represented the sum which he was bound to pay in order to be able to work the colliery. It is contended on behalf of the Department that there is nothing to show that this sum was a charge upon the colliery and that it is possible that the sum was personally due from Kumar Ganesh Singh. Having regard to the usual terms of leases of this nature one is entitled to assume that the assessee was unable to work the colliery without payment of the arrears and that it was incumbent upon him to pay the arrears in order that he might continue working the colliery. If the assessee succeeds in realizing the sum from Kumar Ganesh he would no doubt be liable to pay the tax thereupon, but so long as he is not able to realise the amount from Ganesh Singh he is justified in demanding a deduction on this amount. I am therefore of opinion that the assessee was not liable to taxation under this item and I would answer the question accordingly.

As regards the seventh item, the assessee claims a sum of Rs. 78,000 on account of loss which he alleges he incurred in certain indigo concerns. The Commissioner has found that the assessee has failed to prove such loss. The accounts produced by him are hopelessly unintelligible and it has been found impossible to discover from the accounts whether there has been any loss. The Commissioner, after hearing the appeal against the assessment made by the Income-tax Officer, asked for certain reports from the Income-tax Officer. Before the Income-tax Officer the assessee produced certain accounts. The Income-tax Officer, however, reported that he was still unable to find that there was any loss. On receipt of the report the Commissioner disposed of the appeal without hearing the assessee. It is contended that he was entitled to be heard before the appeal was finally disposed of. The Commissioner says that the assessee was fully heard on his appeal and that no fresh hearing was necessary. It is no doubt an elementary principle of law that no order should be passed against any party in a judicial proceeding without an opportunity being given to that party of being heard. In the present case, however, there were no fresh materials placed before the Commissioner, and the fact that he did not hear the assessee after receipt of the report is not a circumstance which would in any way affect the correctness of the decision of the Commissioner on appeal.

The last point as regards the jurisdiction need not be discussed at any length. It appears that in the present assessment the Commissioner acting under section 5(4) of the Income-tax Act made an order in writing directing that the powers conferred upon the Income-tax Officer and the Assistant Commissioner by or under the Act should be exercised by the Assistant Commissioner and the Commissioner respectively, and accordingly the present assessment was made by the Assistant Commissioner acting as Income-tax Officer. The Assistant Commissioner acting as the Income-tax Officer made the assessment at Patna and it appears that this was done with the consent of the assessee. The question now raised is, that he was not justified under the law in making the assessment at Patna but that he was bound under section 64 of the Act to do so at Darbhanga. Having regard to the circumstances of the case I am of opinion that the contention raised by the assessee cannot be sustained.

I accordingly agree with my Lord the Chief Justice and would answer each of the questions raised in the manner proposed by his Lordship.

[346] *PRIVY COUNCIL.*

ON APPEAL FROM THE HIGH COURT OF JUDICATURE AT BOMBAY.

*Present: Lord Buckmaster, Viscount Dunedin, Lord Tomlin,
Sir George Lowndes and Sir Binod Mitter.*

(26th November, 1929).

The Commissioner of Income-tax, Bombay .. *Appellant**

v.

The Bombay Trust Corporation, Limited, as agent of the
Hongkong Trust Corporation, Limited. .. *Respondent.*

Indian Income-tax Act (XI of 1922), Secs. 42 and 43—Loans by non-resident company to assesseees—Interest remittances—Assesseees, if assessable as agents of non-resident—Business connection, if exists—Agent in Sec. 42, meaning of.

Where the Income-tax Officer after serving a notice under Sec. 43 of the Income-tax Act of his intention to treat the assesseees as agents of a non-resident company to whom they had paid interest on sums of money lent to them on deposit from time to time, assessed them as agents of the non-resident company in respect of the amount of interest,

HELD, that the interest was profit or gains accruing or arising to the non-resident company from a business connection in British India with the meaning of Sec. 42 and that the assesseees were chargeable thereunder as agents of the non-resident company.

The term agent in Sec. 42 of the Act includes a person “deemed to be agent” under Sec. 43 and is not confined to agents in receipt of profits or gains.

Judgment of the High Court reversed.

Appeal [Privy Council Appeal No. 37 of 1929], from a judgment of the High Court of Judicature at Bombay (Marten, C. J., and Kemp, J.), dated the 13th March, 1928 reported as 3 I. T. C. 135.

A. M. Dunne, K.C. and Reginald Hills, for Appellant.

A. M. Latter, K.C. and E. B. Raikes, K.C. for Respondents.

JUDGMENT.

VISCOUNT DUNEDIN:—The respondents in this case are the Bombay Trust Corporation, Limited, who are a company having their office in Bombay. A company called the Hongkong Trust Corporation, incorporated in Hongkong (hereinafter called the Hongkong Company), lent money, from time to time, on deposit to the respondents at the rate of $5\frac{1}{4}$ per cent. and the respondents duly paid interest at that rate on the money deposited. The Senior Income-tax Officer duly served a notice on the respondents in terms of section 43 of the Indian Income-tax Act, 1922, that he intended to treat them as agents of the Hongkong company, and after hearing the respondents as to liability, he assessed them to income-tax and super-tax as agents of the Hongkong company in respect of the amount of interest in the year of charge. The respondents appealed to the Commissioner under section 30 of the Act contending that they were not liable to be so assessed, and also raising questions as to amount. The Commissioner on the hearing of the appeals held that they were properly assessed as

* (1930) 54 Bom 216; 57 I. A. 49; 58 M. L. J. 197; 31 L. W. 583; 34 C. W. N. 230; A. L. R. (1930) P. O. 54.

agents for the Hongkong company, but altered the assessment as to the amount. No further question on the amount arises. The respondents in pursuance of section 66 (2) of the Act required the Income-tax Commissioner to refer to the High Court the questions of law arising out of the decision of the Commissioner.

The questions so referred were as follows:—

“(1) Whether the interest paid by the Bombay Trust Corporation, Ltd., to the Hongkong Trust Corporation, Ltd., on loans taken by the Bombay Trust Corporation, Ltd., is profits or gains accruing or arising to the Hongkong Trust Corporation, Ltd., directly or indirectly through or from any business connection or property in British India.

(2) Whether such interest is liable to income-tax under the Indian Income-tax Act.

(3) Whether the Bombay Trust Corporation, Ltd., can be treated as the agent of the Hongkong Trust Corporation, Ltd., for the purpose of section 42 of the Income-tax Act in respect of the interest so paid by the Bombay Trust Corporation, Ltd., to the Hongkong Trust Corporation, Ltd.

(4) Whether the Bombay Trust Corporation, Ltd., can be deemed to be assessee under section 42 of the Act in respect of any income-tax which might be levied on the interest so paid by the Bombay Trust Corporation, Ltd., to the Hongkong Trust Corporation, Limited.

(5) Whether the relation between the Bombay Trust Corporation, Ltd., and the Hongkong Trust Corporation, Ltd., was not purely that of a borrower and lender and whether the Bombay Trust Corporation, Limited as borrower, could be deemed to be the agent of the lender the Hongkong Trust Corporation, Limited, under sections 42 and 43 of the Income-tax Act in respect of interest payable on such loan and in respect of any income-tax that may be chargeable on such interest”.

The Court answered the questions submitted to them as follows:—

“(1) Yes, from a business connection, but it also arises directly under section 4 (1) and section 6 (iv) & (vi).

(2) Yes.

(3) and (4) No, because the Bombay Company is not in receipt of any such interest on behalf of the Hongkong Company as required by section 40.

(5) The relation between the two Coys. is that of borrower and lender, but having regard to section 43 the Bombay Company, though deemed to be an agent of the Hongkong Company for the purposes of sections 40 and 42, should not be assessed as they were not in receipt of income.”

Appeal has been granted to His Majesty in Council against the above answers. The sections of the Act referred to in the answers are as follows:—

“Section 40. In the case of any guardian, trustee or agent of any person being a minor, lunatic or idiot or residing out of British India (all of which persons are hereinafter in this section included in the term ‘beneficiary’) being in receipt on behalf of such beneficiary of any income, profits or gains

chargeable under this Act, the tax shall be levied upon and recoverable from such guardian, trustee or agent, as the case may be, in like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiary if of full age, sound mind, or resident in British India, and in direct receipt of such income, profits or gains, and all the provisions of this Act shall apply accordingly.

“Section 42 (1). In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax:

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India.

“Section 43. Any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or through whom such person is in the receipt of any income, profits or gains upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person, shall, for all the purposes of this Act, be deemed to be such agent:

Provided that no person shall be deemed to be the agent of a non-resident person unless he has had an opportunity of being heard by the Income-tax Officer as to his liability.”

The High Court were in their Lordships' opinion clearly right in holding that the interest in question was a profit or gain accruing or arising to a person residing out of British India—to wit the Hongkong company—from a business connection in British India, and therefore falling under the words of section 42. But the High Court, noting that the Act goes on to declare that such profits or gains shall be chargeable to income-tax in the name of the agent who shall be deemed to be the assessee in respect of such income-tax, held that the term “agent” was used in the same sense as “agent” is used in section 40, i.e., a person who receives the said profits and gains, and as the respondents, the Bombay Corporation, did not receive the money but on the contrary paid it, they answered questions 3 and 4 in the negative. In the same way they considered that “agent” in section 43 was also over-ridden as regards its meaning by section 40 and only applied to agents in receipt of the profits and gains. Their Lordships are unable to accept this view, as they feel constrained by the explicit words of section 43, which being explicit must rule whatever may be the general considerations as to what the Legislature was minded or was likely to do. Taking the words as they stand: the respondents have a business connection with the Hongkong company and “through them” the company is in receipt of profits or gains. The necessary notice of the intention of the Tax Officer to treat them as agents provided for has been served on them. All this being so, what says the section? They are “for all the purposes of the Act to be deemed to be such agent”. Now one of the purposes of the Act is section 42. They are therefore to be “deemed to be” the agent who is chargeable to income-tax, are deemed to be the assessee, the assessee being in terms of section 2 (2) defined as the person by whom income-tax is payable. Now when a person is “deemed to be” something, the only meaning possible is that whereas he is not in reality that

something the Act of Parliament requires him to be treated as if he were. It follows that although the High Court was perfectly right in holding that if section 42 stood alone "agent" in that section would mean an agent in actual receipt of the profits or gains which were to be assessed, they failed to appreciate that section 43 puts the person who comes within its term artificially into the position of the agent and of assessee under section 42.

Their Lordships will therefore humbly advise His Majesty that this appeal should be allowed and the judgment of the Commissioner restored. The respondents must pay the costs before this Board and in the Courts below.

Solicitor, India Office, Solicitors for Appellant.

Barrow, Rogers and Nevill, Solicitors for Respondents.

(347) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Justice Sir Alan Broadway, Kt., and Mr. Justice Tapp.

(28th November, 1929).

Feroze Shah

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and N. W. F. Province.

Indian Income-tax Act (XI of 1922), Secs. 13 and 66 (3)—Mercantile system of accounting—Absence of profit and loss accounts and stock books—Assessment under Sec. 13, proviso—Flat rate basis of assessment—Questions, if raise points of law.

A finding based on evidence as to the assessee's accounts being kept on the mercantile system is one of fact and none the less so because of the non-maintenance of a profit and loss account and a stock book by the assessee.

The particular manner of computation of profits and gains under the proviso to Sec. 13 of the Income-tax Act is entirely within the discretion of the Income-tax Officer and no point of law can arise unless it can be shown that the discretion has been illegally or arbitrarily exercised.

No question of law arises in the assumption of a particular flat rate of percentage as the basis of profits for assessment to income-tax.

Application [Civil Miscellaneous No. 135 of 1929] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Punjab and N. W. Frontier Province to state a case for the opinion of the High Court.

Bevan Petman, Gobind Das and Badri Das, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

TAPP, J.:—This is an application under sub-section (3) of section 66 of the Income-tax Act, XI of 1922, for an order requiring the Commissioner of Income-tax, to state a case on certain alleged points of law arising out of the assessment made on the petitioner, Khan Sahib Mian Feroze Din Kake Khel of Nowshera (N. W. F. Province) on the profits from his timber business, for the year 1926-27.

The facts briefly are that the Assistant Commissioner found that the method of accounting employed by the petitioner in connection with his timber business was the mercantile system or, in other words, entries were made in the accounts on the date not of receipt of money or expenditure of money but on the date of transactions irrespective of the date of payment. He further found that certain sales aggregating Rs. 90,618-8-0 accounted for in April 1927, i.e., not in the accounting year, had as a matter of fact taken place in March or earlier and consequently he took this sum into account when calculating the profits for assessment of income-tax.

The Commissioner of Income-tax declined to interfere on revision under section 33 and on a further petition under sub-section (2) of section 66 requiring him to refer certain points of law to this Court the Commissioner held that no such points arose and declined to make reference.

The points said to arise are contained in para 6 of the application but these were modified by Mr. Bevan Petman at the hearing and formulated as follows:—

1. That the finding of the Assistant Commissioner of Income-tax that the petitioner kept his accounts in accordance with the mercantile system was not based on any evidence whatever, or in any case was an inconsistent finding,

2. That mere credit entries of sales of timber appearing in the books during the accounting year could not be regarded as including profits accruing in that year, when as a matter of fact the prices of such timber were neither realised nor credited as income during that year and,

3. That there was no legally admissible evidence justifying the Income-tax Officer in estimating the profits at a flat rate of 32½ per cent.

The finding of the Assistant Commissioner that the accounts were maintained on the mercantile system is one of fact and a question of law can only arise out of such a finding if a legitimate and reasonable inference is deducible that such finding is not based on any evidence. Now I am not prepared to hold that such is the case.

The finding of the Assistant Commissioner that the accounts were maintained on the mercantile system was arrived at after an audit of the petitioner's account books which showed that the contention of the petitioner that transactions of sales were only completed and entered when 25 per cent. of the sale money had been paid and bills drawn for the balance, was not correct. Only two transactions of this nature were discovered while other entries showed that this was not the invariable practice. Two specific instances of this kind are mentioned by the Assistant Commissioner in his appellate order.

The contention of Mr. Bevan Petman that two of the features of a mercantile system of accountancy are the maintenance of a profit and loss account

and a stock book, whereas neither is kept by the petitioner. The absence of these would not in my judgment necessarily imply that this was not the method of accounting employed by the petitioner when as a matter of fact this has been found and the finding is based on evidence.

It was admitted that no objection was made to the assessment made for the two preceding years 1924-25 and 1925-26 at a flat rate profit of 32½ per cent. and it does not appear that the accounts on which this profit was computed was kept on any different system to that maintained during 1926-27. Therefore it would seem that the method of accounting was one regularly employed by the petitioner assessee and in the circumstances the proviso to section 13 did not come into operation. Assuming however for the moment that no regular method of accounting was employed it has not been shown in what particular manner the Income-tax Officer acting under the proviso has failed in his computation of the profits. The matter is entirely within the discretion of the Income-tax Officer and unless it can be shown that such discretion had been illegally or arbitrarily exercised no point of law can possibly arise.

For the above reasons I would hold that no question of law arises in regard to the first proposition set forth above.

In my opinion the second point also fails as it is abundantly clear from the order of the Assistant Commissioner that the sales aggregating Rs. 90,618-10-0 were made during the year 1926-27 and were shown in April to avoid their inclusion in the income from the accounting year. Indeed as shown by the Assistant Commissioner the agent of the petitioner admitted before him that bills for the sales made to the Oudh and Rohilkhand Railway had been submitted in March and it is therefore perfectly obvious that the sales must have taken place prior to April. On being asked what difference this particular matter made, Mr. Bevan Petman stated that the inclusion of this amount made the petitioner liable to super-tax. Therein lies the explanation for showing these transactions in April, while they were really concluded prior to that month, and it also affords the real reason for the present petition.

In consequence of the views expressed by me in regard to the first and second points the third does not arise as in the circumstances the application of flat rate of profits on the turnover was justified especially as it was the same which was applied in the two preceding years and no objection was raised. Moreover no question of law in my opinion is involved in assuming a particular flat rate as the basis of profits.

It seems unnecessary to examine the several authorities cited at the bar as to what constitutes a question of law in such cases in view of the conclusions reached by me that the findings of the Assistant Commissioner are pure findings of fact and raise no inference that they are perverse or founded on illegal or inadmissible evidence.

For the above reasons I would dismiss the application with costs.

BROADWAY, J.:—I concur.

(348) IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Blackwell.

(16th December, 1929).

Vallabhdas Murlidhar

.. Assessee.*

v.

The Commissioner of Income-tax, Bombay

.. Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 13—Mercantile system of accounting—Bad debts—Right of assessee to write off—Reasonable time—Question, one of fact.

Where the assessee claimed to write off in his accounts as an irrecoverable debt a loan advanced 12 years prior to the year under assessment to the debtor who adjudged insolvent some 5 years ago had obtained his discharge a year previously and in the absence of any explanation for not writing it off earlier, the Income-tax Officer disallowed the assessee's claim to deduct the said debt as a bad debt,

HELD, that the Income-tax Officer had grounds in fact on which in law he could rightly disallow the claim.

A debt claimed to be deducted as a bad debt ought to have been written off within a fair and reasonable time. While it does not rest with the assessee to say when he can write off a bad debt the Income-tax authorities have no arbitrary discretion to say that a bad debt should be written off in any particular year, the question being one of fact to be decided on the evidence and facts in each case.

Case [Civil Reference No. 10 of 1928], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Bombay, for the opinion of the High Court.

CASE.

Under section 66 (2) of the Income-tax Act, 1922, (hereinafter referred to as the Act) and at the instance of Vallabhdas Murlidhar Shet of Yeola, Nasik District, (hereinafter referred to as the assessee), I have the honour to refer to your Lordships for favour of opinion the questions of law categorically set out in paragraph 12 below referring to the interpretation of sections 3, 10, 24 (1) and 55 of the Act arising out of the appellate order of the Assistant Commissioner of Income-tax, Central Division, passed in the matter of the appeal against the assessment of the above assessee for the financial year 1927-28.

2. As required by your Lordships in the Registrar's letter No. 479, dated the 4th February 1927, this Reference has been drafted in consultation with the Government Solicitor and the Advocate-General.

3. In paragraphs 4 to 9, the facts of the case are given. These have been drafted in consultation with Messrs. Smetham, Byrne and Lambert, Solicitors for the assessee, and have their approval. Para 10 gives the contentions of the assessee as set forth by his solicitors. Paragraph 11 deals with contentions on

behalf of the Crown. In paragraph 12 the questions for the decision of the High Court are given and paragraph 13 gives the opinion of the Commissioner as required by section 66 (2) of the Act.

4. *Facts of the case.* For the financial year 1927-28, the Income-tax Officer, Nasik, by his order dated 1—12—1927 levied an assessment on the assessee on a total income of Rs. 2,37,517 under section 23 (3) of the Act derived from moneylending, house property, business in silk cloth, cotton and cotton seeds and dividends. After deducting Rs. 10,673 on account of income taxed to income-tax at source, income-tax was levied on Rs. 2,26,844 and it amounted to Rs. 21,266-10-0. Super-tax was fixed at Rs. 18,362-1-0 on the above total income. (A copy of the Income-tax Officer's order including the assessment form accompanies as Exhibit A).*

5. The above income was ascertained from the assessee's accounts for the Hindu Samvat year 1982 (beginning on 18—10—1925), as that was his 'previous year' as defined in section 2 (11) of the Act for the purposes of his 1927-28 assessment. In arriving at the above income of Rs. 2,37,517, the Income-tax Officer did not allow a claim for a deduction from it to the extent of Rs. 67,612 on account of a certain bad debt written off in the books of account of the Bombay shop of the assessee. The Bombay shop accounts were kept on the mercantile system and the said amount of Rs. 67,612 appeared as a debt due to the assessee in his balance sheet for the Samvat year 1981, a copy whereof was filed with the Income-tax Officer, Nasik, during the course of the assessment proceedings for the year 1926-27. An English translation of the same accompanies as Exhibit B.* The Income-tax Officer in his order (Exhibit A*) disallowed this item of Rs. 67,612 on the ground *inter alia* that the party from whom the bad debt was due became insolvent some four years back, i.e., in the Hindu Samvat year 1978 or thereabout and that as the assessee knew very well that the amount became irrecoverable then, it ought to have been written off, in the year in which it became bad and should not have been carried forward to the Samvat year 1982 on the basis of which the assessment for 1927-28 was levied as stated above.

6. Against the above assessment, the assessee lodged an appeal to the Assistant Commissioner (Exhibit C*) claiming, among other items, the above bad debt amount of Rs. 67,612. The Assistant Commissioner's finding of facts *re*: this item after hearing the assessee was as under (Exhibit D*) :—"Rs. 67,612 were due from Abhechand Premchand at the end of Samvat year 1969 on account of cotton, gold and silver and Hundi transactions. The debtor declared himself insolvent in 1920 and was discharged some 4 years back. Says nothing was recovered from the insolvent. Thus the total amount actually became irrecoverable to the knowledge of the appellant some 4 years back. Has no answer as to why this amount was not written off in the year when it was known to them that *de facto* this amount had become irrecoverable. The effect of the present write off tantamounts to writing off losses of previous years in the current year's accounts. Accordingly this cannot be allowed."

7. From the above, it will be seen that the Assistant Commissioner's finding was that the amount of Rs. 67,612 became irrecoverable to the knowledge of the assessee some four years back and that as the latter did not write it off in the year in which it became irrecoverable but carried it forward to the Samvat year 1982, it was not allowable.

* Not printed.

8. Under sections 3 and 55 of the Act, income-tax and super-tax are payable on the total income of an assessee for the "previous year" as defined in section 2 (11) of the Act. The "previous year" in this case was Samvat 1982 as stated above. The Income-tax Officer and the Assistant Commissioner were of opinion that as tax was leviable on the result of the year Samvat 1982 only and as the loss of Rs. 67,612 on account of the above bad debt did not arise in 1982 but in some previous year, it could not be taken into account.

9. The assessee thereafter petitioned to me to review the case under section 33 of the Act (Exhibit E*) and allow the above and certain other items. In view of the Assistant Commissioner's finding of fact that the debt became bad to the knowledge of the assessee in the year 1978 Samvat or thereabout and not in 1982 Samvat which finding appeared to be correct, I declined to allow this item (Exhibit F*) following the decision of the Punjab High Court in the case of *Lala Puranmal v. The Commissioner of Income-tax, Punjab* (1). The assessee thereupon requested me to refer to your Lordships for decision the two questions of law categorically set out in paragraph 12 below arising out of the appellate order of the Assistant Commissioner, Central Division, dated the 11th January 1928.

10. The assessee's contentions are—

(a) That it is for him to determine when the debt became irrecoverable and that as he considered it irrecoverable in the Samvat year 1982 and wrote it off as a bad debt in that year, the Income-tax Officer ought to have allowed it when he found it duly written off in the accounts for the Samvat year 1982 and that he cannot decline to allow it simply on the ground that in his opinion it became a bad debt not in 1982 Samvat but in some previous year,

(b) that the only fact proved before the Income-tax Officer was that the said Abhechand Premchand became insolvent some 4 years back. From the said fact, the Income-tax Officer was not entitled to conclude that the debt became in law 'irrecoverable four years back,'

(c) that as the Bombay accounts of the assessee are kept on the mercantile basis system and as he is all along assessed on book profits, the bad debts must be allowed as a deduction from the book profits in the year in which it is actually written off by the assessee in the accounts as irrecoverable.

11. The Crown contends *inter alia* as under:—(a) that the assessee cannot raise at this stage any questions of fact and that the Assistant Commissioner's finding of fact that the debt became bad to his knowledge about 1978 Samvat is binding on him, and (b) that even when the accounts are kept on the mercantile basis, a bad debt must be written off in the year in which it becomes bad and not in any year thereafter as may suit the assessee.

12. *Questions of Law to be decided by the High Court:*—The questions of law which the assessee wants your Lordships to decide are as under as stated by his Solicitors:—

"(1) Whether in the matter of the assessment of the assessee for the year 1927-28, the Income-tax Officer had under the law any discretion to disallow the bad debt of Rs. 67,612 duly written off in the accounts, on the ground that it became bad, not in Samvat year 1982 on the basis of which the above assessment was levied, but four years back.

* Not printed.

(1) 2 I. T. C. 236.

(2) Whether it was not for the assessee to determine when he should write off the above bad debt."

13. *Opinion of the Commissioner*:—Under sections 3 and 55 of the Act, income-tax and super-tax are to be levied on the income, profits and gains of an assessee for the previous year as defined in section 2 (11) of the Act. The previous year in this case was Samvat 1982. As the bad debt in question became bad about the year 1978, as per the finding of fact by the Assistant Commissioner which is binding on the assessee, the loss arose in that year and not in 1982. Hence it could not be allowed while calculating the assessee's income for the latter year. The assessee may carry forward a bad debt and write it off whenever he likes in his accounts but that has nothing to do with the question of a correct calculation of his income for the "previous" year. Tax is to be levied on that income alone under sections 3 and 55 of the Act and so any item of profit or loss for any preceding year which may have been carried forward by an assessee to the "previous" year is not to be taken into account.

14. A copy of your Lordships' decision may kindly be certified to me for further action as required by section 66 (5) of the Act.

Coltman with Messrs. Smetham, Byrne and Lamburt, for the Assessee.

The Advocate-General with the Government Solicitor, for the Crown

JUDGMENT.

MARTEN, C. J.:—The short point in this Reference which we have to decide is whether the assessee was entitled to deduct an alleged bad debt of Rs. 67,612 in his assessment to income-tax and super-tax for the year 1927-28 for the purpose of which assessment he would be assessed under section 3 of the Income-tax Act on his income for 'the previous year' viz., the Hindu year beginning with the 18th October 1925. It is common ground that the debt in question was due from one Abhechand Premchand, and that it arose at the end of S. Y. 1969 (1912-13) on account of transactions in cotton, gold, silver and hundis. It is further common ground that Abhechand Premchand became insolvent in 1920 and that he was discharged in 1924. Further, nothing has been recovered from the insolvent, and in the proceedings before the Assistant Commissioner, no answer was given by the assessee to the question, why this amount of Rs. 67,612 was not written off in or about the year when it was known to have become irrecoverable. The only explanation given by the assessee appears in his Revision Petition to the Commissioner, Exhibit E, of the 19th January 1928 where he submits "that this amount was not written off as the insolvency proceedings were going on, say from 1920 to 1923 or 1924."

Now, it may be taken that the accounts of the assessee are kept on what is known as the mercantile system of accounting, and not on a cash basis. It may also be taken for the purposes of this present Reference that a regular method of accounting was employed by the assessee within the meaning of section 13 of the Income-tax Act, despite certain observations to the contrary as to the earlier years which were made by the Income-tax Officer in the original proceedings before him, Exhibit A.

The main contentions put before us on behalf of the assessee are that it is for him to determine when a debt becomes a bad debt; that he can choose any year he likes for that purpose; and that although in law insolvency may bar the remedy for a debt, yet, it often happens,—particularly amongst Hindus,—

that debts are paid notwithstanding the law of insolvency and notwithstanding the law of limitation. In connection with the last point, two authorities in *Ram Kishan Rai v. Chhedi Rai*(1), and *Gajadhar v. Jagannath*(2), were referred to. Speaking for myself, I think that those authorities are remote from the question which we have to decide, namely, whether in assessing the income, profits or gains of the assessee for the year in question under sections 3, 4 and 10, it was fair and reasonable to deduct this particular bad debt for the year in question. The Assistant Commissioner found that it was not proper to do so, and in revision this finding has been confirmed by the Commissioner. Certain criticisms were passed by Counsel for the assessee to the effect that there has not been a sufficient finding of fact by the Commissioner. But in the result this objection was, I think, withdrawn, and it was expressly stated that it was not desired to refer this case back. In our opinion, the findings in the case are sufficient to show that the Commissioner agreed with the findings by the Assistant Commissioner, and refused to exercise his powers of revision under section 33.

That leaves us with the main point, and here it must be borne in mind that under section 22, it is for the assessee to make a return, but under section 23 (2) the Income-tax Officer can require the assessee to produce evidence, and then under sub-section (3) the Officer assesses the income of the assessee and determines the sum payable by him. Section 24 provides for a set-off for loss. Then sections 30 and 31 provide for an appeal to the Assistant Commissioner who may make such further enquiries as he thinks fit, and may confirm, reduce or enhance the assessment or set it aside. Then section 32 provides for a limited class of appeals against the order of the Assistant Commissioner. That section does not apply in the present case. Then section 33 gives the Commissioner a power of revision,—wrongly called a “power of review” in the marginal note, because, as pointed out by the learned Advocate-General, the corresponding words in section 66 (2) have been amended, so as to read “power of revision under section 33.” Then under section 66, where a question of law arises, the Commissioner may draw up a statement of the case and refer it with his own opinion to us.

In my judgment, the assessee has put his case too high in saying that it rested with him to say when he could write off a bad debt. Speaking for myself, I think that for the purposes of the present case, it is sufficient to say that in law the bad debt in question ought to have been written off within a fair and reasonable time. Adopting that test here, were there grounds in fact on which in law the Commissioner could properly come to the conclusion that it would not be fair and reasonable to write off that bad debt for the year of assessment in question? In my judgment, such grounds clearly existed. The debt in question, as I have already pointed out, had been incurred some 12 years before the year under assessment, the debtor had become insolvent some 5 years previously, and had obtained his discharge over a year before. Under those circumstances, in the absence of any reasonable explanation as to why the debt was not written off before, I would hold that *prima facie* it was unfair and unreasonable in assessing the income for the year in question to write off this old debt, which on any reasonable basis should have been regarded as irrecoverable years before.

On the other hand, I must not be taken to hold that the Commissioner has an arbitrary discretion to say that a bad debt should be written off in any particular year. He or the Assistant Commissioner has to hear the evidence in

(1) (1922) I. L. R. 44 All. 628.

(2) (1924) I. L. R. 46 All. 775.

each particular case and to decide on the facts of that particular case. That I think is one answer to the argument of hardship and so on which was urged before us by counsel for the assessee.

Then we were referred to the decision of the Lahore High Court in *Puran Mal v. The Commissioner of Income-tax, Punjab*, (1). But as the two learned Judges, before whom the case originally came, differed, and the judgment of the third judge proceeds on lines differing somewhat from each of the previous judgments, I do not propose,—with all respect—to refer to the details. I would rather decide the present case on its own facts, and doing that it seems to me that the answer we should give is reasonable and clear.

Accordingly I would answer question 2, namely, “whether it was not for the assessee to determine when he should write off the above bad debt”, by saying, no—not on the facts of this particular case. But as regards question 1 namely,—“whether in the matter of the assessment of the assessee for the year 1927-28, the Income-tax Officer has under the law any discretion to disallow the bad debt of Rs. 67,612 duly written off in the accounts, on the ground that it became bad, not in the Samvat year 1982 on the basis of which the above assessment was levied, but four years back?” I would propose to answer as follows: “In the matter of this assessment the Income-tax Officer had grounds in fact on which in law he could rightly disallow,—as he in fact did,—the bad debt of Rs. 67,612 written off in these accounts.”

In the result, therefore, as we agree with the decision arrived at by the Commissioner, we will direct that the assessee should pay the costs of this reference, to be taxed on the Original Side scale by the Taxing Master.

BLACKWELL, J.:—I agree. In my opinion it is for the assessee in each case to establish by evidence that a debt became irrecoverable during the year in which the income, profits and gains are to be ascertained,—this being a question of fact.

On the facts stated in the present case, I think it clear that the assessee did not establish this by evidence. On the contrary, as appears from Exhibit D to the case, the assessee had no answer to the question why the debt was not written off in the year when it became known to him by reason of the debtor's insolvency that this amount had become irrecoverable. The assessee might, no doubt, have sought to establish by evidence, if such were the case, that, notwithstanding the insolvency of the debtor, the amount did not in fact become irrecoverable until the year in which he wrote it off as a bad debt. But he offered no evidence with a view to establishing this. Accordingly the Assistant Commissioner on the evidence before him found that the debt became irrecoverable some years before it was written off. The Commissioner agreed in this respect with the Assistant Commissioner. In the absence of any evidence by the assessee with a view to establishing that the debt became irrecoverable during the year in question, speaking for myself, I find it difficult to see how the Assistant Commissioner or the Commissioner could have come to any other finding of fact.

I agree that the questions submitted to us should be answered in the manner indicated by the learned Chief Justice.

(349) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice Das and Justice Sir L. C. Adami.

(17th December, 1929).

Panchu Gopal Banerji

... Assessee.

v.

The Commissioner of Income-tax, Behar and Orissa.

Indian Income-tax Act (XI of 1922), Secs. 33 and 66 (2) and (3)—Assessee not applying under Sec. 66 (2)—Application under Sec. 66 (3), maintainability of.

An application to the High Court under Sec. 66 (3) of the Income-tax Act is not maintainable where the assessee without preferring an application to the Commissioner under Sec. 66 (2) applied under Sec. 33 for a review with an alternative prayer for a case to be stated under Sec. 66 (1).

Application [Miscellaneous Judicial Case No. 98 of 1929] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Behar & Orissa to state a case for the opinion of the High Court.

JUDGMENT.

This is an application under section 66, paragraph 3, requiring the Commissioner of Income-tax to state a case to this Court.

Mr. Agarwala on behalf of the Commissioner of Income-tax takes a preliminary objection and it is this. He contends that the Commissioner was not asked by the petitioner to state a case under section 66 (2) of the Income-tax Act and that in these circumstances the present application is not maintainable.

It appears that the petitioner applied to the Commissioner under section 33, invoking his power of review under that section. In his application the petitioner stated that if the Commissioner was unwilling to exercise his power under section 33, he might be pleased to draw a statement of the case and refer it with his own opinion thereon to the High Court under section 66 (1) of the Income-tax Act. This being the position, it is obvious that the present application is not maintainable. The essential condition for such an application is that an application under section 66, paragraph 2 has been made to the Commissioner and refused by him. We must therefore reject the application with costs; hearing fee two gold mohurs.

(350) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Lal Gopal Mukerji and Mr. Justice Bennet.

(19th December, 1929).

Messrs. Basant Rai Takhat Singh

... Assessee.*

v.

The Commissioner of Income-tax, United Provinces.

... Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 9, 10 and 12—Assessee taking lease of lands for one year and sub-letting—Income therefrom, if from property or business—Assessability as from “other sources.”

Where the assessee took a lease of vacant sites from the Agra Cantonment authorities for one year only on specified rent with a covenant not to put permanent structures thereon and sub-leased parcels of the same, with or without the temporary stalls erected by them, to different persons who paid ground rent.

HELD, that the income received by the assessee therefrom was assessable as ‘income from other sources’ under Sec. 12 of the Income-tax Act, the contract with the Cantonment authorities not being ‘property’ or ‘business’ within the meaning of Secs. 9 and 10 of the Act respectively.

Case [Civil Miscellaneous Case No. 794 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

This is an application for reference to the High Court under section 66 (2) of the Income-tax Act.

2. The assessment is that of a Hindu undivided family, which was made in the name of Seth Jaswant Rai in the year 1927-28. Seth Jaswant Rai is now dead, and the application for reference has been made by the heirs Seth Basant Rai and Takhat Singh.

3. The application is in respect of the assessment for the year 1927-28 which was made on an income of Rs. 42,386 from property, vide assessment order, Appendix A.*

4. The assessee holds considerable areas under a lease from the Agra Cantonment authorities, on a portion of which they have constructed their own buildings which are let out on rent. The vacant lands included in the lease are also let out to squatters from whom the assessee realized ground-rent. They have also to pay ground-rent to the Cantonment authorities.

In the year in question the assessee's main sources of income arose from (a) the buildings constructed by them on the land leased from the Agra Cantonment authorities; (b) a portion of the aforesaid leased land which was let out to squatters from whom ground-rent was realized; and (c) a contract for the supply of “bhusa.” They were assessed on their income from property alone as they had suffered loss in the sub-letting of the vacant lands and in the “bhusa” business, and the Income-tax Officer allowed the former loss and set it off against the income from property. He had disallowed the loss claimed to have arisen from the “bhusa” contract which was, however, allowed in appeal, vide Appellate order, Appendix B.*

In the course of the assessment the assessee claimed a deduction of (1) Hundiawan, i.e., interest paid by them for money borrowed for business done in some past years, the exact amount of which has not been specified; and (2) the interest paid on money invested in “bhusa” contract business.

The second item, i.e., the interest claimed as paid on money borrowed for “bhusa” contract business, was not allowed as there was no sufficient evidence on the record to prove it, vide Appellate order, Appendix B.*

The first item was disallowed for the reasons set forth below as given in the assessment order of the Income-tax Officer, Appendix A* :—

“With regard to the question of Hundiawan I might mention that according to the statement made by the assessee in 1925-26 he borrowed the following amounts of money some years previously for the following businesses :—

	Rs.
(1) Achal Singh Takhat Singh grain business ..	50,000
(2) Indo-Foreign Commercial Agency ..	60,000
(3) Takhat Singh Bohra, Jewellers ..	40,000
(4) Silver speculation done by Jaswant Rai in Sambat year 1972 ..	70,000
Total ..	<u>2,20,000</u>

Now, no. (1), the grain business, is done by Achal Singh, brother of Seth Jaswant Rai, who separated from the family in March, 1923, and as admitted by Seth Jaswant Rai, he has since then had nothing to do with his brother's business. As such the Hundiawan paid on money raised for that business cannot now be allowed to the assessee.

As for no. (2), the Indo-Foreign Commercial Agency, it ceased prior to March, 1925, and as such the Hundiawan paid by the assessee on money borrowed for that business cannot be allowed to the assessee.

The jewellery business was started through Takhat Singh Bohra, son of Seth Jaswant Rai, in about 1972 and 1973 and continued until 1981. In respect of the last year, viz., 1980-81, there are merely a few entries on pages 40 and 41 of the rokar produced by the assessee in 1925-26. The business ceased in 1980-81 and as such the Hundiawan on money borrowed for that business is also inadmissible.”

The assessee preferred an appeal to the Assistant Commissioner of Income-tax, who did not interfere with the order of the Income-tax Officer on this point.

5. The assessee has now demanded reference on the following points as mentioned in paragraph 5 of their reference application, Appendix C* :—

“(a) That taking of land from the Cantonment authorities and then sub-letting it to others amounts to business and income, profits or gain earned therefrom shall be chargeable only under the head business within the meaning of the provisions of section 10 of the Indian Income-tax Act, 1922.

(b) That capital borrowed for the purpose of business in one year and interest paid thereon in the subsequent years is an admissible deduction within the meaning of section 10 (2) (iii) of Act XI of 1922.

- (c) That the money borrowed on hundis on the security of the landed properties by placing the title-deeds of the property with the person from whom the money was borrowed, and that, too, that that money was used only in extending, purchasing and building the property, is a clear charge on the property within the meaning of section 9 (1) (iv) of the Indian Income-tax Act XI of 1922."

Point (a) I would restate as follows:—

Where, as in the present case, the assessee has taken land on lease and has erected on a part thereof houses and shops which are let out on rent and has let out the rest to squatters on rent, should the income derived from such rents be assessed under sections 9 and 12 or under section 10 of the Indian Income-tax Act, 1922?

The Commissioner of Income-tax is of opinion that the assessment was properly made under sections 9 and 10.

The point (c) does not arise out of an order under section 31 or section 32 of the Income-tax Act as the point taken in appeal referred to money said to have been borrowed for bhusa contract, whereas the point now raised in the reference refers to money said to have been borrowed for building houses. This is entirely a separate matter and cannot therefore be referred to the High Court.

The second point of law that appears to arise is that contained in point (b) which has been very unhappily worded and has been practically obscured by being couched in very general terms. I have read through the facts of the case carefully and have tried to understand the assessee's point, and I think I have succeeded in doing so. The question of law involved in point (b) is therefore referred for the opinion of the High Court in the following form:— Whether the interest on money borrowed for the purpose of a particular business in some past year, and paid during the "previous year" when the business for which the money was actually borrowed did not exist, is an admissible deduction within the meaning of section 10, clause 2 (iii) of the Income-tax Act?

In the opinion of the Commissioner the answer to the question is in the negative. It is submitted that section 10 (2) (iii) does not contemplate the allowance of interest in respect of capital borrowed for the purposes of a business which has ceased to exist and the profits of which are no longer assessable.

6. Relevant portion of the statement of the case was sent to the petitioner for observation and representation, if any, and a copy of his reply thereto, together with a copy of the Assistant Commissioner of Income-tax, Meerut, *ad interim* order dated September 21, 1928, referred to therein, are enclosed as Appendices D* and E*. I do not propose to make any alteration or addition to what I have already stated

JUDGMENT.

This is a reference by the Commissioner of Income-tax at the instance of Messrs. Basant Rai Takhat Singh of Agra.

It appears that the assesseees are members of a Hindu joint family and are assessed as such. They carried on different kinds of business, but for the present, they have got some house property and they hold a lease from the

Cantonment. The leased property consists mostly of vacant land let out to the assesseees for one year. One of the conditions of the lease is that no permanent structure shall be erected on the land leased and the structure that is erected should be removeable within 12 hours. What the assesseees do is to let out the sites, with or without any shelter constructed by themselves over them to different persons and realise ground rents from the sub-lessees. The Income-tax Officer of Agra assessed the income from the property of the assesseees which consisted of various buildings in various parts of Agra and he also considered the income from the lease as income from property. The result was that, as it was discovered that what was received by the lessees from the land was less than the rent payable to the Cantonment authorities a deduction was made from the income of other house property of the deficit in the contract. The total income from house property came to Rs. 51,000 and odd (after the necessary deductions) and the difference between the rent payable to the Cantonment authorities and the rent realised namely Rs. 9,000 and odd was deducted from the sum of Rs. 51,000 and odd. The assesseees were assessed with a tax on the balance.

The assesseees were not satisfied with this assessment and their grounds were these. They said that the contract obtained from the Cantonment authorities was a 'business' and, further, as they had borrowed certain monies in earlier years for other kinds of business and as they were paying interest on money so borrowed in previous years they should be debited under section 10 (2) (iii) of the Income-tax Act with the interest they had to pay. In other words, they wanted that the interest which they paid should be treated as an outgoing on the head of business and therefore the balance left after deducting the interest from the income, should be treated as their income from the business.

The assesseees wanted that three matters should be referred to the High Court, but the learned Commissioner accepted their prayers as regards two points only. The questions which the Commissioner framed are as follows:—

(a) Where, as in the present case, the assessee has taken land on lease and has erected on a part thereof houses and shops which are let out on rent and has let out the rest to squatters on rent, should the income derived from such rents be assessed under sections 9 and 12, or under section 10 of the Indian Income-tax Act, 1922?

(b) Whether the interest on money borrowed for the purpose of a particular business in some past year, and paid during the "previous year" when the business for which the money was actually borrowed did not exist, is an admissible deduction within the meaning of section 10, clause 2 (iii) of the Income-tax Act?

As regards question (d) on the facts stated by the learned Commissioner himself the language does not appear to be very happy. We understand, and the learned Government Advocate accepts the facts, that the buildings that have been erected on the land leased to the assesseees are entirely of a temporary nature. The buildings cannot be substantial under the terms of the lease itself and therefore the houses and shops that have been erected are mere stalls which are to give shelter to people coming to keep their goods or do other business at the place. The lessees have certain houses, in the proper sense of the word and they have been taxed as property. The property in Anaj Mandi mentioned in the lease at p. 11 of the printed book is not a part of the leased property, the list of which is given at p. 10. For the purposes of our answer, we have to take it, therefore, that several pieces of land belonging to the Cantonment authorities were taken on lease for one year only with the idea that parcels of it should be let

out to sub-lessees for a period not more than one year, and rent should be received from these sub-lessees for the benefit of the lessee. The question then is whether this contract which the lessees obtained from the Cantonment authorities is 'property', or it is 'business'. In our opinion it is neither 'property', nor is it 'business'. The income from this source must come under clause (6) of section 6 of the Income-tax Act and it must be assessed as directed in section 12 of the Income-tax Act. We are of opinion that the income from the contract is to be assessed as income from 'other sources'.

That being our opinion on question (a), question (b) does not at all arise. That question was framed because the Commissioner did not know what the High Court was going to hold on the contention of the parties. As we have held that the income from the contract has to be treated as income from 'other sources' we do not think that we can be properly called upon to pronounce an opinion on a question which does not arise.

We direct that a copy of this judgment be sent to the Commissioner as our answer to the question put by him. The assessee must pay the costs of this reference. We direct that the learned Government Advocate's fee be assessed at Rs. 150 provided he files his certificate of fee within the period allotted.

(351) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Lal Gopal Mukerji and Mr. Justice Bennet.

(2nd January, 1930).

Messrs. Basant Rai Takhat Singh

.. Assesseees.

v.

The Commissioner of Income-tax, United Provinces. .. Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 9 (1) (iv)—Deposit of title deeds outside towns mentioned in Sec. 59, Transfer of Property Act—Charge, if created.

A deposit of title deeds with a creditor outside the towns specified in Sec. 59 of the Transfer of Property Act does not constitute a charge on the properties within the meaning of Sec. 9 (1) (iv) of the Income-tax Act.

Case [Civil Miscellaneous Case No. 794-A of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act, (XI of 1922), by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

This case is referred, under section 66 (2) of the Income-tax Act, for the decision of the High Court.

2. The assessment is that of a Hindu undivided family, which, now in the year 1928-29, stands in the names of Seth Basant Rai and Takhat Singh, as Seth Jaswant Rai, the former head of the family, has died. Seth Basant Rai and Takhat Singh have made this application under section 66 (2) of the Income-tax Act.

3. On January 25, 1929 the Income-tax Officer, Agra, made an assessment for the year 1928-29 on the following incomes:—

					Rs.
(i) Property	...	...	...	...	34,496
(ii) Other sources:—					
					Rs.
(a) Ground-rent	...	6,926			
(b) Interest	...	38			
					6,964
Total					41,460

(It may be mentioned here that the assessment originally made was on a total income of Rs. 41,360, but there was an arithmetical error in the calculation of the income from property which was rectified by the Income-tax Officer on February 2, 1929 under section 35 of the Income-tax Act, and the assessment was framed on a total income of Rs. 41,460).

4. At the time of the assessment the assessee claimed the following two items:—

- (1) A sum of Rs. 25,216 as a deduction from property on account of interest paid to Messrs. Chhotey Lal Abir Chand, Bankers of Agra.
- (2) A sum of Rs. 8,440 on account of litigation expenses as a deduction from the income from ground-rent.

5. As regards the first item, it was alleged that the assessee had borrowed money on hundis from the above-mentioned firm, and as the bankers wanted the assurance that the debtors would not mortgage their property with anyone and insisted on the deposit of the title-deeds with them, they had to do so accordingly. It is said that the deposit of the title-deeds with the creditors constitutes a charge on the property within the meaning of section 9 (iv) of the Income-tax Act.

6. The Income-tax Officer disallowed the first claim in its entirety and allowed a portion of the other claim (vide his assessment order, Appendix A*). The assessee appealed against the order to the Assistant Commissioner of Income-tax, but the order of the Income-tax Officer was upheld (vide Appellate order, dated March 31, 1929, Appendix B*).

7. The assessee has now demanded a reference on the following points, as mentioned in paragraph 7 of their application for reference (vide Appendix D*):—

“(a) That the amount borrowed on hundis on the security of property which was extended, purchased and built from those money and title-deeds of the said property were placed with the person from whom the money was borrowed is a clear charge on the property within the meaning of section 9 (1) (iv) of the Indian Income-tax Act, XI of 1922.

(b) That the amount of entire litigation expenses incurred in one of the business of the assessee (that is, taking land on lease from

the Cantonment authority and then sub-letting it to others is one of the business of the assessee) is an admissible deduction within the meaning of section 10 (2) (ix) of the Indian Income-tax Act, 1922.

- (c) That the taking out of land on lease from the Cantonment authority and then sub-letting it to others amounts to business and income, profits or gain earned therefrom is chargeable to income-tax only under the head business within the meaning of section 10 (1) of the Act, and loss sustained thereunder shall be set off within the meaning of section 24 of the Indian Income-tax Act, 1922.
- (d) That amount borrowed for the purpose of business in one year and interest paid thereon in subsequent years is an admissible deduction within the meaning of section 10 (2) (iii) of Act XI of 1922.
- (e) That no penalty under section 46 (1) or 46 (1-A), can be imposed after issuing warrant of distress to the Collector for recovery of tax under section 46 (2) of the Act, and when the Collector has started the proceedings of recovery thereunder."

8. The point (b) has been withdrawn by the assessee (vide their application dated June 12, 1929, Appendix C*).

The points (c), (d) and (e) were not raised in the appeal made before the Assistant Commissioner of Income-tax under section 31 of the Income-tax Act, and as such do not arise out of an order under section 31 or 32 of the Income-tax Act. They cannot therefore be referred to the High Court.

The only point of law that can be referred, and is referred, for the opinion of the High Court is contained in point (a) and is formulated as under:— Whether the deposit with the creditors of title-deeds relating to property for the purpose of borrowing money for the purchase and extension of property constitutes a charge on the property within the meaning of section 9 (i), clause (iv) of the Indian Income-tax Act, 1922. The answer to the question is, in the opinion of the Commissioner, in the negative.

9. Relevant portion of the statement of the case was sent to the petitioner for observation and representation, if any, and a copy of the relevant portion of his reply thereto is enclosed as Appendix E for the information of the Hon'ble High Court.

JUDGMENT

This is a reference by the Commissioner of Income-tax and the facts involved are briefly as follows:—

There was a joint Hindu family which is now described as Seth Basant Rai Takhat Singh. The family owns certain immovable properties and they have been assessed for the payment of income-tax on the income thereof. The family claims a deduction of a certain amount of money on the ground that that amount was paid by them on account of interest on money borrowed. Their case further is that this money was borrowed on the security of certain title deeds and the transaction constituted a mortgage on the property. They further said that the money had been borrowed in order to extend the property.

The purpose for which the money may have been borrowed would be immaterial. The whole question is whether any charge was created on the property on the income of which the tax has been assessed. The question that has been formulated by the learned Commissioner is as follows:—"Whether the deposit with the creditors of title deeds relating to property for the purpose of borrowing money for the purchase and extension of property constitutes a charge on the property within the meaning of Sec. 9 (i) clause (iv) of the Indian Income-tax Act, 1922". The language employed is not 'very expressive, but we can find out from the assessee's application itself what was their case. The assessee states (at pp. 6 & 7) in their application that they had borrowed money and they had deposited title deeds of the property for the extension of which they had borrowed the money. Again they said: "The amount borrowed on hundis on the security of property which was extended from those money and title deeds of the said property were placed with the person from whom the money was borrowed is a clear charge on the property.....". The whole question for decision is whether the mere fact that certain title deeds were deposited would create a charge on the properties themselves?

Section 100 of the Transfer of Property Act has been relied upon. It says "where immovable property of one person, is by act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property." In this particular case before us, it is not alleged that the property itself was made security for the money borrowed. All that is alleged is that title deeds were deposited. The deposit of title deeds as creating a mortgage has been recognised only in particular cases (see Sec. 59 of the Transfer of Property Act). Where Sec. 59 does not apply there is no rule of law which says that a mere deposit of title deeds should be taken as creating a security on the property to which the title deeds relate. If we had before us a definite contract by which immovable properties had been made security for money borrowed, the matter might have been different. No such case is before us. We are therefore relieved from deciding whether there can be in law a good charge, where it is created or sought to be created by word of mouth. No such question arises and we need not decide it. All that we hold is that a mere deposit of title deeds outside the towns mentioned in Sec. 59 of the Transfer of Property Act will not amount to creation of charge on the properties to which the deeds relate.

The result is that our answer to the question is in the negative.

Let a copy of this judgment be sent to the Commissioner of Income-tax for his information. The learned Government Advocate is entitled to a fee of Rs. 100 provided he files his certificate, within the time allowed by the rules. The assessee will pay costs of this reference.

(352) IN THE HIGH COURT OF JUDICATURE AT BOMBAY.

Before Sir Amberson Marten, Kt., Chief Justice and Mr. Justice Blackwell.

(8th January, 1930).

Raja Bahadur Bansilal Motilal

.. Assessee.*

v.

The Commissioner of Income-tax, Bombay.

.. Referring Officer.

* I. L. R. 54 Bom. 460; 1930 (A. I. R.) Bom 581.

Indian Income-tax Act, (XI of 1922), Secs. 4 (1), 8 and 18 (4)—Government Promissory Notes issued and repayable in British India—Enfacement for payment of interest at Hyderabad (Deccan)—Interest received at Hyderabad—Assessability to super-tax—Scope of Secs. 8 and 18 (4).

Interest received by the assessee at Hyderabad (Deccan) on Government of India Promissory Notes issued and repayable in British India and enfaced for payment of interest at Hyderabad (Deccan) Treasury, accrued or arose in British India within the meaning of Sec. 4 (1) of the Income-tax Act and is assessable to super-tax.

Secs. 8 and 18 (4), of the Act are not confined to interest receivable or deemed to be received in British India.

Case [Civil Reference No. 4 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Bombay for the opinion of the High Court.

CASE.

Under section 66 (2) of the Indian Income-tax Act, XI of 1922, (hereinafter referred to as "The Act") and at the instance of Rajah Bahadur Bansilal Motilal (hereinafter referred to as "the assessee"), I have the honour to refer for your Lordship's decision the questions of law categorically set out in paragraph 12 below which have arisen out of the super-tax assessment of the above assessee for the financial year 1927-28. These questions as well as the facts of the case enumerated in paras. 2 to 11 below have been approved by the assessee's Solicitors, Messrs. Merwanji Kola & Co., and the Reference has been drafted in consultation with the law advisers of the Crown as required by Your Lordships in the Registrar's letter No. 479 of 4th February, 1927.

2. *Facts of the case*:—For the financial year 1927-28, the assessee's total income was assessed by the Income-tax Officer, A-Ward, Bombay, at Rs. 3,47,469 as per his Assessment Order dated 24th February 1928, a copy of which is appended hereto as Exhibit A*. A copy of the assessment form dated 28th February 1928, pertaining to this assessment is also annexed hereto as Exhibit B*. The amount of super-tax payable on the above total income of Rs. 3,47,469 was Rs. 40,071-6-0 after deducting the statutory allowance of Rs. 75,000 from it, the assessee being a joint Hindu family.

3. The assessment as per Exhibits A* and B* included a sum of Rs. 87,015 on account of interest on Government Promissory Notes and other securities. A part of this interest to the extent of Rs. 73,515 was taken by the Income-tax Officer to be in respect of securities liable to income-tax, the rest amounting to Rs. 13,500 being in respect of securities on which interest was free from income-tax though liable to super-tax.

4. This said sum of Rs. 87,015 was represented before and was accepted by the Income-tax Officer and the Assistant Commissioner as being the amount of interest on Government of India Promissory Notes and other securities paid to the assessee through the Residency Treasury at Hyderabad, Deccan. The assessee contended that (1) as this interest was paid outside British India, (i.e., at Hyderabad), and (2) as the Government of India Promissory Notes in respect of which it was paid were enfaced for payment at the Hyderabad Treasury, it was not liable to either income-tax or super-tax. The Income-tax Officer, however, did not allow this contention and assessed the assessee as per his order Exhibit A* and demanded super-tax as stated above.

5. Against the said assessment, the assessee by his petition dated the 27th March 1928, appealed to the Assistant Commissioner of Income-tax claiming *inter alia* that he was not liable to be assessed on the said sum of Rs. 87,015 forming a part of his total income on the following grounds:—

“The petitioner is not liable to be assessed on the following items: (a) Interest on Government securities Rs. 87,015. The interest was not received in British India, nor has it accrued or arisen in British India and the same cannot be assessed. The Promissory Notes of the Government of India were enfaced for payment at the Hyderabad Deccan Treasury which is out of British India. That this was a contract under the Government Securities Act and hence neither income-tax nor super-tax is leviable in the event which accrued due and was received at Hyderabad Deccan. The petitioner claims to be entitled to a refund of the income-tax wrongfully deducted at source at Hyderabad. Without prejudice to the above, the petitioner submits that the wrongful deduction of income-tax at the source at Hyderabad does not make the petitioner liable for super-tax”.

A copy of the said petition dated 27th March, 1928 is annexed hereto and marked Exhibit C.*

6. The Assistant Commissioner having taken into consideration the said petition and heard the representatives of the assessee did not revise the assessment but by his order dated 8th October 1928 confirmed the same. A copy of the said order is hereto annexed and marked Exhibit D.* The reasons given by the Assistant Commissioner for rejecting the claim put forward are stated by him as under:—

“The test whether interest on certain securities of the Government of India, which are not issued free of tax, is liable to income-tax or not is a simple one, viz., whether there is a right to receive such interest in British India or not. In the present case, the right to receive payment of interest is a right to receive it in British India; hence the income accrues in British India, whether it be actually received in British India or not. The mere enfacement for payment of interest at Hyderabad (Deccan) Treasury does not exempt such interest from income-tax or super-tax”.

7. Against the said Order, the assessee by his letter dated the 6th November, 1928, applied to me to refer to this Honourable Court the questions set out in para. 12 below. Copies of the said application for a reference and of the two enclosures thereto [viz., (1) a statement of facts and (2) the questions to be referred] as also of the Solicitors' covering letter thereto are hereto annexed and marked collectively as Exhibit E.* The Solicitors also requested me at the same time to grant them the necessary relief under section 33 of the Act and to send on the Reference to the Honourable Court in case I was unable to do so. As I am unable to give any relief to the assessee under section 33 of the Act, I am submitting this Reference for your Lordships' decision.

8. In order to give your Lordships a clear idea as to how an enfacement for the payment of interest from a particular treasury is made on a promissory note, I submit herewith a copy of one such note (marked as Exhibit F*) recently purchased by the assessee and forwarded to me by him for this purpose.

9. On going through the papers of the case, I found that the records contained no proof as regards the following facts alleged on behalf of the petitioner and taken for granted by the lower authorities, viz., (1) that the whole of

* Not printed.

the interest amounting to Rs. 87,015 was paid from the Hyderabad Residency Treasury and was received by the assessee at Hyderabad and (2) that the Promissory Notes in respect of which this interest was paid were enfaced for payment of interest at Hyderabad.

As regards (1), evidence has now been produced before me which shows that only Rs. 51,948-8-0 out of the sum of Rs. 87,015 claimed were actually paid at Hyderabad and that the rest of the interest was paid in Bombay. The Solicitors for the assessee have agreed that the sum of Rs. 51,948-8-0 is the correct amount of interest drawn at Hyderabad and not Rs. 87,015 as claimed before the lower authorities.

10. As regards (2), this may be accepted although no direct evidence is available as the securities on account of which the interest was drawn at Hyderabad have been sold by the assessee. Certificates issued by the Treasury Officer, Hyderabad Residency Treasury, have been produced from which it may be presumed that the interest was drawn at Hyderabad and that the notes were enfaced for payment of interest at Hyderabad.

11. In support of their contention, the assessee's Solicitors rely on Rule 9 framed under section 24 of the Indian Securities Act, 1920, (X of 1920, India), which runs as under: "Interest on a Government Promissory Note shall be paid at any Treasury or Sub-Treasury for payment of interest at which the note has been enfaced, but only on presentation of the note itself and on signature by the payee of a receipt in Form IV. Where, however, interest on a Government Promissory Note is payable at Calcutta, or a Government Promissory Note is enfaced for payment of interest at Bombay or Madras, the note itself shall be presented at the Local Public Debt Office which shall issue interest warrants in favour of the holders payable at the local Head Office of the Imperial Bank of India."

12. *Questions for decision of the High Court.*—The questions which the assessee has asked me to submit to your Lordships for determination are "(1) Whether the interest received by the assessee at Hyderabad (Deccan) on Government of India Promissory Loan Notes enfaced for payment at Hyderabad (Deccan) Treasury can be said or deemed to accrue, or arise, or to be received in British India within the meaning of section (4) (1) of the Act, (2) Whether the said interest is liable to be assessed to super-tax".

13. *Opinion of the Commissioner.*—As section 66 (2) of the Act requires me to give my opinion while referring the case to the Court, I beg to state that in my opinion the answer to the above questions should be as under:—1. The interest income accrues and arises in British India. 2. Yes.

14. A copy of your Lordships' decision may kindly be certified to me for further action as required by section 66 (5) of the Act.

Sir Chimanlal Setalwad, B. J. Desai and Tanaporewala, instructed by Messrs. Merwanji, Kela & Co., for the Assessee.

Sir Jamshed Kanga, Advocate-General, with A. Kirke-Smith, Government Solicitor, for the Crown.

JUDGMENT.

MARTEN, C. J.:—The two questions submitted to us under section 66 of the Indian Income-tax Act 1922 are as follows:—1. Whether the interest received by the assessee at Hyderabad (Deccan) on Government of India Promissory Loan Notes enfaced for payment at Hyderabad (Deccan) Treasury can be said or deemed to accrue, or arise, or to be received in British India within the meaning of section 4 (1) of the Act.

2. Whether the said interest is liable to be assessed to super-tax. Admittedly the second question depends on the answer to the first having regard to section 56 of the Act

The amended Exhibit F is a specimen copy of one of the Promissory Notes of the 4½ per cent. Loan 1955-60 in question. This Note was originally issued by the Government of India to the Imperial Bank of India in British India, and is dated the 15th September 1928. The principal and interest were both payable at Calcutta, the former between 1955 and 1960, and the latter half-yearly at 4½ per cent. per annum. The Promissory Note was then assigned to the assessee by the Bank and was duly endorsed in his favour. It was also "enfaced"—as it is called—by the direction that the interest was payable at Hyderabad (Deccan). This enfacement was effected under certain statutory Rules framed by virtue of the Indian Securities Act 1920. It had the effect of making the interest thenceforth payable at the Hyderabad Residency Treasury, which, though an office of the Government of India, has now been expressly found by the Commissioner to be situate outside British India. No point has been taken that the date of the enfacement, viz., 7th August 1928, is prior to that of the Promissory Note itself. Admittedly Exhibit F is only a specimen, as the original Promissory Notes have since been sold by the assessee and parted with. So I pass that by. Accordingly we have to deal with a case where at the material dates the debt was contracted in British India, and the principal was repayable in British India, but the interim interest on such principal was payable outside British India.

Turning next to the Indian Income-tax Act, 1922, section 4 (1) runs as follows:—"Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing, or arising or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India". Section 4 (2) deals with certain business profits accruing or arising outside British India which are nevertheless to be deemed to have accrued or arisen there. But that sub-section does not apply here. Section 6 makes "interest on securities" taxable, and section 8 provides that the tax shall be payable by an assessee under that heading "in respect of the interest *receivable* by him on any security of the Government of India or of.....etc." Section 18 (1) provides that as regards interest on securities, tax shall be leviable in advance by deduction at the time of payment. Section 18 (4) provides that all sums so deducted "shall for the purpose of computing the income of an assessee, be deemed to be income received." In the present case tax was deducted as provided by this section.

It will be seen that the more important words in section 4 (1) are "all income.....as.....comprised in section 6 from whatever source derived, accruing, or arising or received in British India." Now in the first place I think it clear that the use of the word "or" means what it says, and that accordingly the two expressions "accruing or arising" are different from the expression "received", and are intended to catch income which would not necessarily be received in British India. I also think that these expressions "accruing or arising" indicate some origin or source of growth for the income in question. Thus Murray's Dictionary defines "accrue" to mean "*(inter alia)* arise or spring as a natural growth especially interest. "To grow or arise as the produce of money invested." Some analogy may also be found from Lord Cairn's well-known description of an English Railway Debenture as being charged only on the produce of "a fruit-bearing tree," viz., the tolls and fares only of the capital undertaking. (See *Gardner v. London Chatham and Dover Railway Com-*

pany(1). And indeed in this very clause 4 (1), we have the earlier words "income.....from whatever source derived."

Now the interest we have to deal with clearly arose or sprang from principal moneys invested in British India and repayable in British India. Its amount was calculated as a percentage on those principal moneys, and its source was those principal moneys. And if this interest had also been payable in British India, then normally it would have been caught by section 4 (1) as being "received" there, quite apart from any other words. But the argument of the assessee to be successful must take this vital step, viz., that because the interest was in fact payable outside British India, and received outside British India, therefore it did not accrue or arise in British India. In my judgment that argument is unsound. It in effect confines the words "accruing or arising" to "payable", and ignores the fact that income payable in British India is normally caught by the word "received". It also ignores what I have already mentioned as to the origin or source of the interest. In short this argument treats the sole test as being where is the income payable.

The matter does not, however, entirely rest there. We have also to consider the effect of sections 6, 8 and 18 of the Act, for the income in question may fall within all these sections. It was argued for the assessee that the word "receivable" in section 8 was only intended to prevent any assessee from escaping tax by omitting to obtain actual payment of the interest, and then urging that he had not "received" this income within section 4. I do not however think that this is the only effect of this word "receivable", for under section 18 (1) the tax would be deducted at the source, and by section 18 (4) it would "be deemed to be income received". But, however that may be, I do not think that in the case of securities of the Government of India, sections 8 and 18 (4) have the effect of confining the interest in question to interest receivable in British India or "deemed to be received" there. The words "in British India" do not appear in those sections. Accordingly, provided the income in question accrues or arises in British India within section 4, I think it is liable to tax although receivable or received outside British India. Under these circumstances it is unnecessary to decide whether the assessee would be liable under section 8 alone, on the ground that it applies to interest wherever receivable on securities of the Government of India. The main charging section is section 4 (1), and that is the section referred to in the questions submitted to us, and I think rightly so, for the income to be taxed must be brought within its ambit.

As regards the authorities cited to us, they are not, I think, directly in point in the present case. The English authorities depend on the English Act which is worded differently from the Indian Act, and enacts a different basis of taxation from that in India, which depends on income accruing or arising or received in British India or deemed so to be [See *Rogers Pyatt Shellac and Company v. Secretary of State for India* (2), and *Board of Revenue, Madras v. Ramanadhan Chetty* (3)]. The Indian authorities brought to our attention were on quite different facts. Accordingly in this respect I do not propose to add anything to the judgment of my brother Blackwell, which I have had the advantage of reading.

In the result I would hold that the income in question being interest on a security and debt of the Government of India issued and contracted in British

(1) (1866-67) L. R. 2 Ch. App. 201 at p. 207.

(2) 1 I. T. C. 863 at pp. 868 & 869.

(3) 1 I. T. C. 37 at p. 41.

India and repayable there, accrued or arose in British India within the meaning of section 4 (1) of the Act, notwithstanding that it was actually payable and paid outside British India. I would, therefore, uphold the opinion of the Commissioner, and answer the questions submitted to us as follows, viz., (1) The interest in question is income accruing or arising in British India within the meaning of section 4 (1) of the Act. (2) The said interest is liable to be assessed to super-tax. I would also direct the assessee to pay the Commissioner's costs of this Reference, to be taxed by the Taxing Master on the Original Side scale.

BLACKWELL, J.:—The answers to the questions submitted on this reference depend upon the meaning to be attributed to the words in section 4 (1) of the Income-tax Act 1922, "income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing or arising, or received in British India".

The learned Counsel for the assessee drew our attention to the judgments of the Court of Appeal in *Colquhoun v. Brooks*(1), Dealing with the true construction of Schedule D in 16 and 17 Victoria, Chapter 34, Lopes L. J., said: "I understand the words 'arising, or accruing to any person residing in the United Kingdom' to mean coming to his hands or received by him in the United Kingdom." An argument that this was the proper meaning to be attributed to the words "arising or accruing to any person residing in the United Kingdom" was advanced in the House of Lords, but it was not accepted by Lord Macnaghten who said: "Nor is there, I think, any room for the argument that the expression 'arising or accruing to any person', in the first sentence of Schedule D means 'received' by any person in the United Kingdom" (see 14 Appeal Cases at page 511). In section 4 (1) of the Indian Income-tax Act of 1922 the words "accruing or arising" are found in juxtaposition to the words "or received". Accordingly I think it plain that the words "accruing or arising" denote something different from the word "received".

It was next contended on behalf of the assessee that the interest on these Government of India Promissory Notes did not accrue or arise in British India, because that interest, by virtue of the enfacement made upon the notes, is payable at a place outside British India. It was argued that the income must accrue or arise to the assessee, that the source or place from which the income was derived was immaterial, that the assessee had no right to demand payment of the interest on these notes in British India, and that the interest did not therefore accrue or arise to him in British India.

In support of this argument Counsel for the assessee drew our attention to an expression of opinion in the dissenting judgment of Fry L. J. in *Colquhoun v. Brooks*(1), as follows:—"I think, therefore, that the words 'arising or accruing' are general words descriptive of a right to receive profits". Counsel for the assessee submitted that this interpretation of these words was correct, and that income, profits or gains can be said to accrue or arise only in the place where there is a right to receive them. But in the case in question Mr. Brooks undoubtedly had the right to receive the profits in Australia, where they were made, as well as the right to bring them to England, if he chose. These words of the Lord Justice cannot therefore in my opinion be relied upon as an expression of opinion that profits or gains do not arise or accrue in the place where they are made.

(1) 2 Tax Cas 490 ; 14 App. Cas 493.

Turning to the Indian authorities to which our attention was drawn, not much assistance can in my opinion be derived from them, the facts in each case being so different from those in the present. There are, however, certain passages in some of the judgments in those cases, to which I will briefly refer, which appear to me to be opposed to the contentions raised on behalf of the assessee in the present case.

In *Board of Revenue, Madras v. Ramamadhan Chetty* (1), Abdur Rahim, Offg. Chief Justice, said at page 41 with reference to section 3 (1) of the Income-tax Act of 1918 (which corresponds in substance with section 4 (1) of the present Act):—"The tax is leviable with reference to the place where the income accrues or arises or is received, and not with reference to the residence of the person who is entitled to receive the income". In the same case at page 44 Seshagiri Ayyar, J. refers to "the *situs* of personal property for the purposes of taxation" as being "of the utmost importance in determining the limitation of the taxing power and the principles which should control the exercise of that power". The learned Judge goes on to say that the English Income-tax Acts appear to have been based on this principle, and after quoting a passage from the judgment of Lord Herschall in *Colquhoun v. Brooks* (2), as follows:—"the Income-tax Acts, however, themselves impose a territorial limit; either that from which the taxable income is derived must be situate in the United Kingdom or the person whose income is to be taxed must be resident there", he says that the same principle is traceable in the provisions of the Indian Income-tax Acts; and at page 45, in discussing the scheme of the Act of 1918, he says:—"There is first a general provision as to the *locale* of the income which is to be taxed. That is contained in section 3, clause (1)."

Again, in *The Secretary to the Board of Revenue, Madras, v. Arunachalam Chettiar* (3), Wallis, C. J., in discussing section 3 of the Act of 1918, said at page 77:—"That section which appears under the head of 'Taxable income' provides in effect that the income which is to be taxed under the Act is income from whatever source derived if it accrues, or arises, or if it is received in British India, that is to say, income which accrues or arises in British India is taxable even if it is received elsewhere as in England, while income which is received in India is taxable even if it accrued or arose out of British India." I respectfully agree with these expressions of opinion by these learned Judges, which are equally applicable to the words used in section 4 (1) of the present Act. I think that the words "accruing or arising" are used with reference to the place from which the income is derived, and the use of the word "source" in the expression "from whatever source derived" confirms me in this opinion. In the present case the interest is derived from a loan which was made in British India, that loan, as to the principal, being re-payable in British India, and I entertain no doubt that the interest accruing due upon, or arising from, that loan accrues or arises in British India.

But even if this interest accrues or arises in British India, must there still be a right to receive it in British India in order to render the payee liable to income-tax and super-tax? I think not. This class of income falls within the second head mentioned in section 6 of the present Act, namely, "Interest on Securities." Section 8 provides as to this class of income as follows:—"The tax shall be payable by an assessee under the head 'Interest on Securities' in respect of the interest receivable by him on any security of the Government of India or of a Local Government. The word used here is 'receivable'. It is not

(1) 1 I. T. C. 37.

(3) 1 I.T.C. 75.

(2) 2 Tax. Cas. 490.

confined to interest which is receivable in British India. Accordingly, in my opinion the tax is payable upon this interest, which I hold to accrue or arise in British India, notwithstanding that the assessee has no right to receive it in British India, and that it is receivable at a place outside British India.

I would therefore answer the questions submitted as follows:—(1) The interest accrues or arises in British India and (2) The said interest is liable to be assessed to super-tax.

Per Curiam. Answer the questions as follows: (1) The interest is income accruing or arising in British India within the meaning of section 4 (1) of the Act. (2) The said interest is liable to be assessed to super-tax. Order the assessee to pay the Commissioner's costs of this Reference to be taxed by the Taxing Master on the Original Side scale.

(353) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Ormiston and
Mr. Justice Brown.*

(10th January, 1930).

P. K. N. P. R. Chettyar Firm

.. Assessee.*

v.

The Commissioner of Income-tax, Burma.

.. Referring Officer.

Indian Income-tax Act (XI of 1922) Secs. 23 (4), 27 and 66 (2)—Failure to comply with Note 5 of return—Application to reopen assessment—Sufficiency of cause—Discretion of the Income-tax Officer, scope and limits of—Reference to High Court—Question not referred, if arguable.

In deciding the question as to the sufficiency of cause under Sec. 27 of the Income-tax Act, the Income-tax Officer must not, in the exercise of his discretion, act capriciously, arbitrarily or in an unsound manner.

Where the Income-tax Officer rejected an application under Sec. 27 of the Income-tax Act to reopen an assessment under Sec. 23 (4) for failure to comply with the provisions of Note 5 of the Return form, the only reason submitted for the default being the practice of not keeping Chettyar accounts on a yearly basis

HELD, that the discretion given by Sec. 27 was properly exercised by the Income-tax Officer.

On a reference under Sec. 66 (2) it is not open to the assessee to raise before the High Court any question other than that referred.

Case [Civil Reference No. 11 of 1929] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Burma, for the opinion of the High Court.

CASE.

In accordance with the order in Civil Miscellaneous Application No. 10 of 1929,* dated the 16th July 1929, the following case is stated for the decision of the High Court under the provisions of section 66 (3) of the Income-tax Act.

2. The assessee is a Hindu undivided family carrying on a money-lending business by an agent in the Ma-ubin District. For the assessment for 1927-28 the agent in response to a notice under section 22 (2) submitted a form of return declaring an income of Rs. 34,000 as the income of the business for the previous year. No statement as required by Note 5 of the form showing how the figure of income declared had been arrived at was attached. This requirement is prescribed by Rule 19 of the Income-tax Rules which are statutory rules. The omission was pointed out to the agent by the Income-tax Officer, but it was not remedied. The Income-tax Officer then, acting under section 22 (4), called for the complete accounts of the business. Account books were produced but the Income-tax Officer found that certain *bakki* books had been withheld. For this default and for the default in respect of the return the Income-tax Officer made the assessment under section 23 (4). This section provides:—"If the principal officer of any company or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment."

The assessee then applied under section 27 of the Act for the reopening of the assessment. As regards the return, he stated that it was not practicable to furnish the statement required since Chettyar accounts were not maintained on a yearly basis, and as regards the accounts, he contended that no *bakki* books were kept for the business. The Income-tax Officer rejected the application, taking the view that the requirement in respect of the return was a statutory requirement which could not be dispensed with and still believing that *bakki* books were maintained. The assessee appealed to the Assistant Commissioner under section 30 against this order. The Assistant Commissioner conceded that it might be true that in this case *bakki* books were not maintained and decided in favour of the assessee as regards this alleged default. He held, however, that the assessment was properly made under section 23 (4) as the form submitted by the assessee was not a valid return. He declined to consider any question touching the merits of the assessment since having held that the assessment was properly made under section 23 (4) he had no jurisdiction in the matter, an appeal against the assessment being barred by the proviso to section 30 (1).

The assessee then submitted to the Commissioner applications under section 66 (2) and section 33 of the Act. In the application under section 66 (2) three questions were submitted for reference to the High Court. The first question concerned the validity of the return. This matter having been settled by this High Court in the case of *A. R. A. N. Chettyar v. Commissioner of In-*

* Reported as 4 I.T.C. 87.

come-tax(1) my predecessor declined to refer it. The second question concerned the jurisdiction of the Assistant Commissioner in respect of an assessment made under section 23 (4). This question was not referred in view of the decision of the Allahabad High Court in the case of *Jhuri Misra v. Commissioner of Income-tax, United Provinces*.(2) The third question which disputed the reasonableness of the assessment was held to be a question of fact and not of law. The application under section 66 (2) was rejected, and after reviewing the proceedings my predecessor declined to interfere in the assessee's behalf under section 33. A copy of the order under section 66 (2) is attached,—Annexure "A."

3. The assessee then made an application to the High Court under section 66 (3). In the order of the High Court referred to in paragraph 1 I am directed to state a case on the following point:—"Whether or not the discretion given by section 27 was properly exercised in this case."

Section 27 of the Act is as follows:—"Where an assessee or, in the case of a company, the principal officer thereof, within one month from the service of a notice of demand issued as hereinafter provided, satisfies the Income-tax Officer that he was prevented by sufficient cause from making the return required by section 22, or that he did not receive the notice issued under sub-section (4) of section 22, or sub-section (2) of section 23, or that he had not a reasonable opportunity to comply, or was prevented by sufficient cause from complying, with the terms of the last mentioned notices, the Income-tax Officer shall cancel the assessment and proceed to make a fresh assessment in accordance with the provisions of section 23."

As the only default which is now in issue is the failure to file a valid return, all that need be considered is whether in respect of this default the Income-tax Officer exercised in a sound and reasonable manner the discretion given to him by section 27 to reject the assessee's application. The assessee made the following statement in his application under section 27:—"It is a time-honoured practice among Chettyars community to close their accounts only at the end of every three years, that is, at the termination of an agency and no interim profit and loss statement is prepared." He goes on to state that it is the practice for the Income-tax authorities to call for accounts and to base the assessment on the accounts. This was the only explanation offered for the default. If this explanation has to be accepted Note 5 (a) or (b) would lose all meaning so far as the assessments of Chettyars are concerned. And if the law prescribes that an assessee who keeps accounts, as the assessee does, must give the details required by Note 5 (a) or (b), how can the Income-tax Officer be said to have improperly exercised his discretion if he insists on compliance with the law? And further, since for the purposes of an assessment if it is to be based on the accounts the requisite figures for the accounting year must be extracted from the accounts, is it too much to expect, as the law expects, that the assessee shall extract these figures himself instead of leaving it to the Income-tax Officer to extract them? In the *A. R. A. N. Chettyar* case referred to in paragraph 2, this Hon'ble Court held that a return which did not comply with the requirements of Note 5 was not a valid return. It was impossible, therefore, for the Income-tax Officer, in view of this ruling and after specifically drawing the assessee's attention to the requirement in question, to accept the contention of the assessee.

My opinion therefore on the question formulated by the High Court is that the discretion given by section 27 was properly exercised in this case. To hold otherwise would, in my opinion, mean a direction to Income-tax Officers that they should go out of their way to dispense with the requirements of the law.

Hay with Venkatram, for the Assessee.

Government Advocate, for the Crown.

JUDGMENT

ORMISTON, J.:—The assessee, a Hindu undivided family carrying on a money lending business, being thereunto required by a notice under section 22 (2) of the Indian Income-tax Act, submitted a form of return declaring an income of Rs. 34,000 as the income for the previous year. Rule 19 of the Rules made by the Board of Inland Revenue, in exercise of the powers conferred by section 59 of the Act, provides that the return of total income for Hindu undivided families shall be in the form therein prescribed, which is headed statement of total income during the previous year. To the form are appended certain notes. Note 5 (a) is "when you keep your accounts on the mercantile accountancy or book profits system, you must file return in the following form." Then follows the form. Rule 5 (b) is "where you do not keep your accounts in such a form you must file a statement showing how you arrive at the taxable profits." The Notes are part of the rule and have as much validity as the statement of total income above referred to. Section 59 (5) of the Act declares that rules made under the section, when published in the Gazette of India, shall have effect as if enacted in the Act.

Admittedly the assessee filed neither a return under Note 5 (a) nor a statement under Note 5 (b). The Income-tax Officer then, acting under section 22 (4) called for complete accounts of the business. Books were filed. The Income-tax Officer was of the opinion that the assessee had suppressed certain books, and for this default and for the default in respect of the return, made the assessment under section 23 (4) to the best of his judgment. The assessee then applied to the Income-tax Officer under section 27. That section, so far as relevant, provides that where an assessee satisfies the Income-tax Officer that he was prevented by sufficient cause from making the return required by section 22, the Income-tax Officer shall cancel the assessment and make a fresh assessment. The Income-tax Officer refused to make a fresh assessment, and the assessee under section 30 appealed against such refusal to the Assistant Commissioner. The Assistant Commissioner, while deciding in favour of the assessee on the question of the books, was of the opinion that the return made under section 22 (2) was not in accordance with the statutory requirements, and, (under section 31), refused to set aside the assessment made under section 23 (4). The assessee then applied to the Commissioner under sections 66 (2) and 33. The Commissioner refused, under section 33, to interfere on the assessee's behalf and, being of the opinion that no question of law arose, rejected the application under section 66 (2). Application was then made in Civil Miscellaneous No. 10 of 1929. This Court, differing from the Commissioner, held that a question of law, namely, whether or not the discretion given by section 27 was properly exercised, arose out of the Assistant Commissioner's order under section 31, and required the Commissioner to state a case and refer it to the Court. The Commissioner has accordingly referred the following question, "Whether or not the discretion given by section 27 was properly exercised in this case."

The question referred has not been argued. Mr. Hay contended that, the reference having been made, it was open to him to argue any question of law which might be considered to arise and that he was not confined to the question referred. The only authority cited for this proposition is *S. P. K. A. A. M. Chettyar Firm v. Commissioner of Income-tax, Burma*(1). The particular question of law decided in that case related to the validity of an assessment under section 23 (4), it being there held that, because the assess-

ment in question was entirely arbitrary, it was illegal. We have referred to the record of that case and it appears that the question there referred was, "Whether the Income-tax authorities acted legally in assessing the applicant under section 23 (4)." This involves two questions, the first being whether the authorities ought to have applied section 23 (4), and the second being whether the assessment made by the authorities under that section was in fact according to the best of their judgment. The second question was in fact referred and it was open to the Court to answer it. The case is, therefore, no authority for Mr. Hay's contention that he is entitled to argue a question other than that referred, and he has put forward no argument in its favour.

The language of sub-sections (2), (3) and (5) of section 66 appears to be against it. Under sub-section (2) the assessee may require the Commissioner to refer to the Court "any question of law arising out of" an order. Thereupon the Commissioner is to state the case and refer it. But he may refuse to state it on the ground that no question of law is involved. If he does so refuse, it is open to the Court, under sub-section (3), to require him to state the case and refer it. If the reference is under sub-section (2) the reference is of a question of law required by the assessee to be stated. In that case it could hardly be contended that it was open to the assessee to argue any question which he had not required the Commissioner to state. The same principle should apply when it is the Court which requires the Commissioner to make the reference and to state the case. Sub-section (5) is even more conclusive. The High Court upon the hearing of any case referred to it "shall decide the questions of law raised thereby." I am of the opinion, therefore, that it is not open to the assessee to raise before the Court any question other than that referred.

The question which Mr. Hay desired to raise is whether the assessment in the present case is in fact arbitrary and, therefore, illegal. The question actually referred, as to whether the discretion under section 27 was properly exercised in this case has, as I have said, not been argued by counsel. It may be very shortly answered. In *S. P. K. A. A. M. Chettyar Firm v. Commissioner of Income-tax, Burma*(1) it was stated with reference to an assessment by an Income-tax Officer to the best of his judgment, that "he must make it according to the rules of reason and justice, not according to private opinion, according to law and not humour, and that the assessment is to be not arbitrary, vague and fanciful, but legal and regular." It was held that the assessment in question was illegal, because it was entirely arbitrary and did not purport to be founded on any materials or reasons beyond the Income-tax Officer's private opinion.

I am of opinion that the same principles are applicable to the exercise of the discretion under section 27. The Income-tax Officer has to be satisfied that the assessee was prevented by sufficient cause from making the return required by section 22. The Income-tax Officer under section 27 has a discretion. This discretion consists of a power to decide whether the cause shown is or is not sufficient. He must not decide this question capriciously, arbitrarily or in a manner which is unsound. There was a statutory obligation on the part of the assessee to comply with the requirements of Note 5 sub-joined to the return and he did not comply with those requirements. His only reason for his default was that he was unable to do so because Chettyars' accounts in general and his in particular were not kept on a yearly basis. The obvious reply to this is that it would have been possible for him by taking sufficient trouble to have extracted such information from his own books as would have enabled

(1) 4 I.T.C. 182.

him to construct a profit and loss account for the preceding year and thus to have put himself into a position to comply with the imperative provisions of the law. On the face of it, therefore, he had not shown sufficient cause for non-compliance with the requirements of Note 5, and the Income-tax Officer was justified in so holding. I would answer the question referred that the discretion given by section 27 was properly exercised in this case.

The order on the application to compel the Commissioner to state a case directed that the costs thereof should abide the final order for costs to be made on the reference. The Commissioner was wrong in refusing to state a case and refer a question of law on the request of the assessee. I would order him to pay to the assessee the costs of that application, advocate's fee Rs. 85. The question of law having now been decided in favour of the Commissioner, I would order the assessee to pay to the Commissioner the costs of the reference, advocate's fee Rs. 85.

RUTLEDGE, C. J.:—I agree.

BROWN, J.:—I agree.

(354) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Mr. Justice Beasley, Chief Justice, Justice Sir V. Ramesam, Kt.,
Mr. Justice Krishnan Pandalai, Mr. Justice Eddy and Mr. Justice Cornish.*

(20th January, 1930).

S. A. S. Subbiah Iyer

.. Assessee*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer

*Indian Income-tax Act, (XI of 1922), Secs. 4 (2), 66 (1), (2) and (5)—
Application for reference—Jurisdiction to direct Commissioner to refer ques-
tions of law not raised—Case stated, Right to argue questions not referred—
Foreign remittances, nature of presumption as to—Remittances entered in
accounts as capital—User of remittances, relevancy of—Character of remittances,
Question one of mixed law and fact.*

*Neither under section 66 (1) of the Income-tax Act, nor under Section 45
of the Specific Relief Act can an assessee move the High Court to direct the Com-
missioner to refer a question of law not raised by the assessee before the Com-
missioner by an application under section 66 (2) of the Act.*

*On a case stated by the Commissioner, the assessee is not entitled to argue
before the High Court a question of law though arising out of the assessment
which the assessee did not ask the Commissioner to refer. But the High Court
can, if it chooses, alter the questions referred by the Commissioner or reject them
altogether and decide the real question at issue between the Commissioner and
assessee at the time when the application was made to him to refer the question or
questions.*

*Thiruvengada Mudaliar v. Commissioner of Income-tax, 2 I. T. C. 514;
A. K. A. C. T. Chettyar Firm v. Commissioner of Income-tax, Burma—3 I. T. C.
213 In re Ishar Das Dharam Chand, 2. I. T. C. 12; Approved. Siva Prasad*

* (1930) 58 M.L.J. 581; A.I.R. (1930) Mad. 449.

Gupta v. Commissioner of Income-tax, United Provinces, 3 I. T. C. 406; Referred to.

Whether money remitted to British India from a foreign business is a remittance of profits is a mixed question of law and fact.

The assessee carrying on money lending business in British India and in places outside British India used to remit money to his foreign businesses from British India as well as to receive money from them, there being a continuous flow of money in both directions by means of hundies. In the assessee's account books the remittances from the foreign business were entered as remittances of capital and not of profit, there being a separate profit account. The accounts were found to be genuine accounts honestly kept by the assessee. The Income-tax Officer assessed a portion of the remittances from the foreign businesses as were utilised by the assessee to repay loans borrowed by him in British India as remittances of profit under section 4 (2) on the ground that the sums so assessed were utilised by the assessee to repay loans borrowed by him in British India and that in the absence of separate funds kept in his foreign business for his capital and profits, the remittances must be presumed to be remittances of the available foreign profits.

HELD, that in the circumstances of this case the presumption of the remittances being from out of foreign profits has been rebutted.

The character of a foreign remittance as one of capital or profit is not altered by the use which it is put to on its receipt in British India.

Scottish Provident Institution v. Allan, 4 Tax Cas. 191; A. V. P. M. R. M. Murugappa Chettiar v. The Commissioner of Income-tax, Madras, 2 I. T. C. 139; Explained.

Per Krishnan Pandalai, J.:—*The proper legal inference from admitted facts is a question of law.*

Case (O. P. No. 180 of 1928) stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras in compliance with the order of the High Court.

CASE.

In accordance with the High Court's order quoted above I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3).

2. The petitioner is a resident of Tinnevely carrying on money lending business in Tinnevely and in various other places outside British India of which Quilon in the Travancore State is one.

3. The petitioner was assessed for the year 1926-27 on an income of Rs. 68,395 as given below, the year of account being the Andu year 1100, i.e., the year ended 16th August, 1925.

	Rs.
Income from property	200
Income from other sources (remittances from petitioner's foreign business)	69,473
	<hr/>
Total Rs. ..	69,673
Less loss in petitioner's Tinnevely business ..	1,278
	<hr/>
Total Rs. ..	68,395

The Income-tax Officer calculated the amount of remittances of foreign profits as follows:

	Rs.
Drawings from petitioner's Tinnevelly shop (there were no profits in this shop and there were large remittances from the foreign branches to this shop)	21,469
Amount drawn from Quilon for purchases of lands in Tenkasi taluk	43,810
Amount drawn from Quilon branch by debit to assessee's drawings account for purchase of lands	4,000
Amount received from Quilon in the shape of articles ..	194
Total Rs. ..	<u>69,473</u>

The Income-tax Officer found that the profits of the petitioner's foreign businesses for the Andu years 1097 to 1100 amounted to Rs. 1,99,185 and held that the sum of Rs. 69,473 should be regarded as a remittance out of profits and accordingly included it in the petitioner's assessment.

4. The petitioner appealed to the Assistant Commissioner against the above assessment. An examination of the petitioner's accounts by the Assistant Commissioner showed that during the year of account the petitioner had drawn Rs. 89,847 to his Tinnevelly shop from his foreign businesses in excess of the amounts sent by him to those businesses. As this sum which was larger than the sum which the Income-tax Officer regarded as a remittance of foreign profits, viz., Rs. 21,469 had also been applied in part towards the discharge of borrowings by the petitioner for his Tinnevelly business, the Assistant Commissioner held that the whole amount should be regarded as a remittance of profit and he accordingly enhanced the petitioner's assessment by Rs. 68,378, being the difference between Rs. 89,847 and Rs. 21,469. He also upheld the Income-tax Officer's inclusion in the petitioner's assessment of the sum of Rs. 43,810 being the value of lands in British India taken over by the petitioner in satisfaction of a debt advanced by the petitioner's Quilon business. A copy of the Assistant Commissioner's order is filed marked Exhibit A.*

5. Against the Assistant Commissioner's order of enhancement the petitioner preferred an appeal to my predecessor under section 32. My predecessor after a careful consideration of the facts of this case came to the conclusion that that proportion only of the remittances which had been applied either towards the petitioner's personal expenses or towards the repayment of money borrowed for the purposes of the Tinnevelly business had to be regarded as an appropriation in British India of the profits from abroad. Such proportion came to Rs. 67,209. He accordingly substituted this figure for the Assistant Commissioner's figure of Rs. 89,847. A copy of his order is filed marked Exhibit B.*

6. The petitioner thereupon applied to my predecessor to refer to the High Court the following question:—"Whether or not Rs. 67,209 can be taxed as a remittance of foreign profits under section 4 (2) of the Income-tax Act in the facts and circumstances of this case?" My predecessor declined to make a reference as he considered that the question raised was not one of law. A copy of his order is filed marked Exhibit C.*

7. On the petitioner's application to the High Court under section 66 (3) the High Court has by its order dated 24th April, 1929, directed me to state a case on the 3 following questions:—

Question (1). Whether a sale and conveyance by a debtor of the assessee in respect of money lending business carried on by the assessee out of British India in discharge of the principal and interest of debt due to such business, of lands situate in British India amounts to a remittance into British India of profits of the assessee made in that foreign business.

Question (2) Whether the presumption as to foreign remittances being from out of the profits is applicable or available in a case where the dealings between the British and the foreign businesses consist of large sums of money being lent out by the British Indian business to the foreign business and of such loans being more or less regularly repaid by remittances by the foreign business.

Question (3) Whether the said presumption is applicable or available in a case where the moneys remitted are in the current dealings account and debited to such account and not to the personal or profits account of the assessee and where interest earned every year by the British Indian business in respect of such dealings is included in the assessment of the British Indian business.

8. One of these questions, *viz.*, question (1) was not submitted to me by the petitioner for reference to the High Court and the High Court accordingly in its order in which it directs me to make the reference has stated that the question whether the reference on this point lies at all in law (as not having been stated by the party for reference before the Commissioner) shall be left open for decision by the Bench which hears the reference.

9. Before I proceed to give my opinion on the questions as directed by the High Court I respectfully venture to submit that neither under section 66 (3) of the Income-tax Act, nor under section 45 of the Specific Relief Act is the petitioner entitled to move the High Court for an order directing the Commissioner to refer a question which the petitioner did not raise before the Commissioner under section 66 (2). Sub-sections (2) and (3) of section 66 run as follows:—(2) “Within one month.....an assessee may.....require the Commissioner to refer to the High Court any question of law arising out of such order.....” (3) “If on any application being made under sub-section (2) the Commissioner refuses to state a case on the ground that no question of law arises an assessee may apply within 6 months from the date on which he is served with notice of the refusal to the High Court and the High Court if it is not satisfied of the correctness of the Commissioner's decision may require the Commissioner to state a case and refer it and on receipt of any such requisition the Commissioner shall state and refer the case accordingly.”

The conditions precedent to a motion under section 66 (3) are, therefore, that the petitioner should have asked the Commissioner to refer a question of law to the High Court and that the Commissioner should have refused to refer it. Several questions of law may arise out of an order, but the question on which the reference is demanded must obviously have reference to a matter concerning which the assessee and the Department continue to be at variance. Clearly no useful object is served by the Commissioner making a reference on a point about which there is no longer any dispute. When there is a dispute between the assessee and the Department the assessee at the time when he files his application for a reference to the High Court does not as a rule leave the Commissioner in doubt as to what he is objecting to. When therefore an assessee is silent on any matter concerning which it was open to him to

demand a reference the Commissioner is in my opinion amply justified in presuming that no dispute exists in regard to that particular matter and that consequently no reference on any question of law arising out of that matter is called for. I submit, therefore, that it is necessary when an assessee demands a reference on a question of law that he should indicate in some manner what the matter in dispute is and what the question of law that it gives rise to. When this is done the Commissioner is able to focus his attention on the specified points in dispute and it is open to him in a proper case to exercise the power vested in him to decide the question in favour of the assessee; but this he cannot do when the assessee gives no indication whatsoever as to the points on which he is still at issue with the Department. In the present case the only point raised by the petitioner before the Commissioner in his application under section 66 (2) related to the taxability of the sum of Rs. 67,209, while the question now under discussion relates to an entirely different sum of Rs. 43,810. There was thus no question either of law or of fact raised before the Commissioner in regard to this sum. In my opinion, therefore, he is not entitled to seek any relief from the High Court in regard to this particular point under section 66 (3).

Nor is he entitled to any relief under section 45 of the Specific Relief Act. An application under that section must, according to section 46 of the Act, be founded on an affidavit stating, among other matters, the petitioner's demand for justice and the denial thereof. As I have already observed, the petitioner never demanded a reference on the question and the Commissioner never refused his request. Further, section 45 of the Specific Relief Act can only be invoked when "the applicant has no other specific and adequate legal remedy" (proviso (d) to the section), and it cannot be said that the remedy provided in section 66 of the Income-tax Act is not specific and adequate. The petitioner has therefore no remedy under the Specific Relief Act.

10. Subject to the above objection, I give below my opinion on the questions raised.

Question 1. The facts regarding this point appear to be as follows:—In the year of account the assessee took over certain lands in the Tenkasi taluk of the Tinnevely District in British India in satisfaction of loans advanced by the petitioner's Quilon business. The Income-tax Officer considered the value of these lands taxable as a remittance of foreign profits as the petitioner had received money's worth in British India in the shape of lands and as there were enough profits in the petitioner's foreign concerns. The Assistant Commissioner agreed with the Income-tax Officer's conclusion. As observed in the preceding paragraph I had no opportunity to look into this question. I however consider that the decision of the authorities below was right. The Quilon business is the petitioner's own and in return for money advanced from that business the petitioner has acquired lands in British India. The sale deed has been executed in his name and the property is situate in British India. The debts due to the petitioner's Quilon business formed part of the floating assets of that business. These debts were realised on their conversion into immovable property and the realisation took place in British India. The petitioner thus on the date of the sale of the land became possessed in British India of something of value which he did not possess in that country before. It is clear from these facts that what took place amounted to a receipt of value into British India from Quilon. The floating assets in Quilon consisted both of capital and profits and it was not proved, nor was it even contended, that the remittance in question was not a remittance of profits.

It appears that this land continues to be shown as an asset of the Quilon business but that does not in my opinion affect the question whether its value has

not been received in British India. The substance of the transaction decides the matter and not the manner in which the petitioner may record the transaction in his books. By the purchase of this land there has undoubtedly been a transfer of property from Quilon to British India and such a transfer amounts to a remittance which must be presumed to be profits as the contrary has not been proved. I would therefore request your Lordships to answer the question accordingly.

Question 2. I must observe in the first place that even if the flow of money from Tinnevelly to the foreign shops and *vice versa* could be regarded as loans and repayments there is no reason why the repayments should not have come out of the profits of the foreign business. In fact when a man borrows money to use it for the purpose of making profits and after making the profits repays the loan the most reasonable presumption would be to hold that the repayment of the loan was made out of the profits. This is just what one would expect in the ordinary course of human conduct. I would however point out that it is incorrect in this case to describe the advances of money from Tinnevelly to the foreign shops as loans or the remittances from those shops to Tinnevelly as repayments, for the foreign shops belong exclusively to the petitioner. What happens is merely that sums are sent by the petitioner from Tinnevelly for employment in his own foreign shops where they get mixed with the profits and other funds of those shops and that when remittances are made from those shops to Tinnevelly they come from out of those mixed funds. No particular remittance is sent specifically against, or is identifiable as the return, of, any particular advance. In the year of account under consideration the remittances thus made out of the mixed funds have been utilised in Tinnevelly partly in repaying the loans taken at Tinnevelly for the conduct of the Tinnevelly business and partly for the personal expenses of the petitioner. It is such proportion of the remittances as can be said to have been utilised for these purposes that has been taxed. I respectfully submit therefore that the question as framed does not arise on the facts of this case. The only question that can arise is whether there is anything in the facts of this case to render the presumption regarding foreign remittances being out of profits inapplicable to it. I do not consider that there are any circumstances in this case which render that presumption inapplicable.

Whether a sum remitted is out of profits or not is entirely a question of fact the onus of proving which lies on the petitioner. The petitioner has not discharged that onus and the presumption that the remittances were from profits therefore operates. And indeed the inference is strengthened by the circumstances that the remittances have been applied, to the extent to which they have been taxed, to the repayment of loans borrowed for the use of the Tinnevelly business and towards the personal expenses of the petitioner.

Question 3. The petitioner's reasons for his contention that the remittances are not remittances of profits are two, *viz.*, 1. that the remittances are debited to the Tinnevelly current account in the Quilon books and not to the profit account, and 2. that Tinnevelly charges interest to the foreign business on current advances. The petitioner charges interest on the amounts advanced to his foreign businesses apparently for the purposes of ascertaining whether these businesses are able to work at a profit or not after bearing these interest charges.

The fact that the petitioner debits the remittances to a particular account is not, in my opinion, a sufficient reason for holding that the remittances were not remittances of profits. One has to look to the substance of the transactions and the way in which the petitioner makes entries in his accounts cannot conclude the question of the nature of these transactions. The fact that the petitioner's Tinnevelly shop, for its own accounting purposes, charges interest on its advances to the foreign shop is also, in my opinion, not relevant to the consideration of the

question whether the remittances are remittances of profit or not. My opinion on this question is that the presumption that remittances are out of profits is applicable to this case notwithstanding the fact that the petitioner debits these remittances to particular accounts and charges interest on transactions between the British Indian and the foreign businesses.

V. V. Srinivasa Ayyangar and *P. R. Srinivasan* for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE:—In accordance with the order of the High Court dated the 24th April, 1929 three questions have been referred to the High Court under section 66 (3) of the Indian Income-tax Act by the Commissioner of Income-tax, Madras. Those questions are (1) whether a sale and conveyance by a debtor of the assessee in respect of a money lending business carried on by the assessee out of British India in discharge of the principal and interest of debt due to such business of lands situate in British India amounts to a remittance into British India of profits of the assessee made in that foreign business, (2) whether the presumption as to foreign remittances being from out of the profits is applicable or available in a case where the dealings between the British and the foreign businesses consist of large sums of money being more or less regularly repaid by remittances by the foreign business and (3) whether the said presumption is applicable or available in a case where the moneys remitted are in the current dealings account and debited to such account and not to the personal or profits account of the assessee and where interest earned every year by the British Indian business in respect of such dealings is included in the assessment of the British Indian business.

Question (1) was not submitted to the Commissioner of Income-tax for reference to the High Court when the assessee under section 66 (2) of the Indian Income-tax Act required the Commissioner to refer the other two questions to the High Court; and the High Court in directing the Commissioner of Income-tax to refer all the three questions reserved to the Commissioner the right to contend that the reference on the first point did not lie at all by reason of the fact of its not having been submitted to him under section 66 (2) of the Act. That question was fully argued on the reference. The Commissioner by his order on the petitioner's application dated the 23rd February, 1928 stated that his request could not be granted, that section 66 (1) had no application and that the petitioner could have preferred an application under section 66 (2) but did not do so. Admittedly, the petitioner did not prefer an application under section 66 (2) but Mr. V. V. Srinivasa Ayyangar contends that the High Court can nevertheless require the Commissioner to refer the question under section 66 (1) if the question raises an important point of law for decision. He further contends that, even if section 66 (1) has no application, then under section 45 of the Specific Relief Act the High Court can decide the question.

On the former question he relies upon a decision of the Privy Council in *Alcock Ashdown and Company, Ltd., v. Chief Revenue Authority of Bombay* (1) in that case it was held that it is the duty of the Chief Revenue Authority under section 51 of the Indian Income-tax Act, 1918, to state a case and refer it to the High Court when in the course of an assessment a serious question of law arises. On page 226 Lord Phillimore stated, "In their Lordships' view always supposing that there is a serious point of law to be considered, there does lie a duty upon

the Chief Revenue Authority to state a case for the opinion of the Court, and if he does not appreciate that there is such a serious point, it is in the power of the Court to control him and to order him to state a case." It was argued that section 51 of the Indian Income-tax Act of 1918 is similar to section 66 of the present Act, namely, the Indian Income-tax Act of 1922. Section 51 of the Indian Income-tax Act of 1918 is as follows:—If in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VII, a question has arisen with reference to the interpretation of any of the provisions of this Act or of any rule thereunder the Chief Revenue Authority may, either on its own motion or on reference from any Revenue Officer subordinate to it, draw up a statement of the case and refer it, with its own opinion thereon, to the High Court, and shall so refer any such question on the application of the assessee, unless it is satisfied that the application is frivolous or that a reference is unnecessary.

We do not agree that that section is similar to section 66 of the present Act. Under section 51 (1) of the Act of 1918 the assessee could apply to the Chief Revenue Authority to refer any such question and he was not limited in that section as to the time in which he had to make his application. Section 66(2) of the present Act requires the assessee to make his application within one month of the passing of the order under section 31 or section 32 and further more requires that application to be accompanied by a fee of Rs. 100 or any such lesser sum as may be prescribed. Mr. Sreenivasa Ayyangar's contention is that the assessee has two remedies open to him, one under section 66 (1) and another under section 66 (2). We are unable to accept that contention. It is most unlikely that the legislature intended to give an assessee two remedies one within a specified limit of time and another without any such limitation. It cannot seriously be argued that after an order has been made an assessee who has neglected to make an application to the Commissioner to refer a question of law arising out of that order within one month of the making of that order can nevertheless, many months afterwards, ask the Court to require the Commissioner of Income-tax to refer the same question to the High Court merely because it is one of importance. Moreover it is clear that section 66 (1) is not intended to benefit an assessee but is merely to enable the Commissioner when he feels any difficulty with regard to a question of law to refer the matter himself to the High Court. The assessee, therefore, not having made his application to the Commissioner to refer question (1) to the High Court within one month of the passing of his order, cannot ask the High Court to direct the Commissioner to refer such a question.

It was also contended on behalf of the assessee that any point of law arising out of the facts of the case can be taken cognizance of by the High Court and an opinion given upon it because section 66 says that the Commissioner is to draw up a statement of the case and it is contended that this means the whole case i.e., the whole assessment. In support of this contention *Shiva Prasad Gupta v. Commissioner of Income-tax, U. P.* (1) was referred to. There it was decided that though ordinarily the Income-tax Commissioner would be the officer who would frame the points of law that arise in the case stated by him and though he would be expected to give his own opinion on those points of law for the benefit of the High Court section 66 requires the High Court to decide the questions of law that arise in the case i.e., the High Court is entitled to "resettle the issues" as it were and to decide those issues. On page 413 Mukerji J. states:—"The meaning and object, however, of the entire section 66 seems to me to be free from obscurity. My impression is that the High Court has to accept the facts as found by the Commissioner of Income-tax and if necessary may call for more facts by asking him to make a fresh statement of them under sub-section 4, section 66. But it is

for the High Court to find out from the contention of the assessee on the one hand and the contention of the Income-tax authorities on the other, what is the real point of law that arises between the parties and what it has to decide. This reading of section 66 seems to be clear to me from among other matters the fact that the High Court is nowhere called upon to decide such questions as may be framed by the Commissioner of Income-tax."

In my view this decision does not mean that the assessee is entitled to argue any question of law which may arise out of the assessment and which he has not asked the Commissioner of Income-tax to refer to the High Court but merely means that the High Court can, if it chooses, alter the question referred by the Commissioner of Income-tax or reject them altogether and decide the real questions of law at issue between the Commissioner and the assessee at the time when application was made to him to refer the question or questions.

This question has also been considered by a Full Bench of this Court in *Thiruvengada Mudaliar v. The Commissioner of Income-tax, Madras*(1) and it was there held that if a point of law is not raised before the Commissioner of Income-tax within the time specified by section 66 (2) of the Indian Income-tax Act it cannot be raised at all and the Commissioner cannot be required to state a case to the High Court raising that question. It was because the correctness of this decision was questioned that this present reference was directed to be heard by a Bench of five Judges. In my view that decision was correct. In *A. K. A. C. T. V. Chettiyyar Firm v. The Commissioner of Income-tax*(2) and in *In the matter of Ishar Das Dharam Chand* (3) a decision of the Lahore High Court, a similar view was taken.

Obviously section 45 of the Specific Relief Act is of no avail to the assessee because by sub-section (d) of that section it is subject to the proviso that the applicant has no other specific and adequate legal remedy. In this case a remedy is provided by section 66 (2) of the Indian Income-tax Act of 1922 but the assessee neglected to avail himself of it. The assessee therefore cannot be permitted to argue the point of law raised in question (1) and it is unnecessary to state any of the facts out of which that point of law emerges.

With regard to questions (2) and (3), the answer to question (2) answers question (3). I, however, think that question (2) does not really raise the question we have to decide. As it stands, the answer clearly must be in the negative. The real question is whether the ordinary presumption that money is one which can be rebutted and what facts rebut it. Mr. Patanjali Sastri in the course of his argument was driven to take up the attitude that it would not be rebutted although he was bound to admit in the earlier stages of his argument that such a presumption could be. He further contended that if it could be rebutted it was purely a question of fact whether it had been rebutted. I think this is a mixed question of fact and law and that obviously such a presumption can be rebutted, the onus of doing so being upon the assessee.

The facts are that the petitioner is a resident of Tinnevely carrying a money lending business in Tinnevely and various other places outside British India of which Quilon in the Travancore State is one. The petitioner was assessed for the year 1926-27 on an income of Rs. 68,395 the year of account

(1) 2 I.T.C. 514.

(2) 3 I.T.C. 213.

(3) 2 I.T.C. 12.

being the year ending the 16th August 1925. The details of the assessment were as follows:—

	Rs.
Income from property	200
Income from other sources (remittances from petitioner's foreign business)	69,473
	<hr/>
Total Rs. ..	69,673
Less Loss in petitioner's Tinnevelly business	1,278
	<hr/>
Total Rs. ..	68,395
	<hr/>

The amount of remittances of foreign profits was calculated by the Income-tax Officer as follows:—

	Rs.
Drawings from petitioner's Tinnevelly shop (there were no profits in this shop and there were large remittances from the foreign branches to this shop) ..	21,469
Amount drawn from Quilon for purchases of lands in Tenkasi Taluk	43,810
Amount drawn from Quilon branch by debit to assessee's drawings account for purchase of lands	4,000
Amount received from Quilon in the shape of articles ..	194
	<hr/>
Total Rs. ..	69,473
	<hr/>

The Income-tax Officer found that the profits of the petitioner's foreign business for the year amounted to Rs. 1,99,185 and held that the sum of Rs. 69,473 should be regarded as a remittance out of profits and accordingly included it in the petitioner's assessment.

From this assessment the petitioner appealed to the Assistant Commissioner and it was found that during the year of account the petitioner had drawn Rs. 89,847 from his foreign businesses in excess of the amount sent by him to those businesses. The petitioner's course of business was to supply his foreign business with money from Tinnevelly. This money he himself borrowed from other persons. The money sent by the petitioner to his foreign businesses was sent by means of hundies and money remitted from those foreign businesses to Tinnevelly was also sent by means of hundies. There was a continuous flow of money during the year in both directions. The Tinnevelly business made no profits in the year of account. The Assistant Commissioner held that as the money received from the foreign businesses was in excess of that sent by the petitioner to those foreign businesses, the excess should be regarded as a remittance of foreign profits. He enhanced the assessment by Rs. 68,378 by taking the excess figure of Rs. 89,847 and deducting from it a sum of Rs. 21,469 which had been applied in part by the petitioner towards the discharge of borrowings by him in his Tinnevelly business. The petitioner then preferred an appeal to the Commissioner of Income-tax against the Assistant Commissioner's order of enhancement and succeeded in reducing the assessment. The petitioner applied to him to refer the following question, namely, "Whether or not Rs. 67,209 can be taxed as a remittance of

foreign profits under section 4 (2) of the Income-tax Act in the facts and circumstances of this case." The Commissioner of Income-tax declined to refer that question being of the opinion that it was not one of law. He was however directed to refer the question to the High Court and it has come up in the shape of questions (2) and (3).

If an assessee's foreign business remits money to him in a country in which his profits from his business in that country are assessed to income-tax, the presumption is that the remittance is a remittance from out of the profits of the foreign business. (*The Scottish Provident Institution v. John Allan*(1) followed in *A. V. P. M. R. M. Murugappa Chettiar v. Commissioner of Income-tax, Madras*(2). In the latter case it was decided that money remitted to the headquarters of a firm in British India from a branch situated in a foreign country is presumed to be profits and not capital and is assessable to income-tax as profits unless the assessee proves the contrary. The Commissioner of Income-tax argues that the assessee has mixed up his accounts of capital account in Quilon, a current account and a profit account and that in his books there is no separate fund kept in respect of these items. It is admitted by him that these remittances from the current account in Quilon are shown in that account to be remittances from capital and are similarly shown in the Tinnevely books to be received in the shape of capital. It is argued that nevertheless the remittances were not from capital at all but were from profits because it is shown that there were profits earned by the foreign business to an amount more than enough to repay the loans received from Tinnevely and that no businessman would be likely to remit capital when he has profits out of which he can repay the loans, and in this contention he is supported by the observations made in *Allan's* case. In the report of that case 4 Tax Cases on page 419, Lord McLaren stated: "But, where a capitalist company, as in the present case, has invested large sums for a period of 15 years in a Colony, and has an agent employed not only to receive interest but also to receive the capital of the investment when paid up and to reinvest it even if unappropriated remittances are made to this country, I think every one would agree that they must be dealt with according to the ordinary course of business and these remittances must be presumed to be paid in the first place out of interest so far as they are income, and in the second place out of principal or capital. I think that rule results from the fact that no prudent man of business will encroach upon his capital for investment when he had income uninvested lying at his disposal."

The Commissioner's contention goes to the length of saying that a businessman is not to be allowed to conduct his own business as he chooses. In the present case the Commissioner of Income-tax agrees that the assessee has acted perfectly honestly, that is to say, he intended to remit capital and not profits from Quilon to Tinnevely and kept genuine accounts and made true entries in those accounts but contends that nevertheless as profits were earned in the assessee's foreign business those remittances must be held to be from those profits and not to be capital. It seems to me clear that, as the Commissioner of Income-tax admits that the assessee acted honestly in making the entries in the account books and had a *bona fide* intention of remitting capital and not profits, his argument that the sums remitted are liable to be taxed must at once fail, and I am far from saying that the assessee did what a prudent man of business would not do. He had borrowed money in Tinnevely for the purpose of lending it out to his foreign business and to make a profit on it and what he had borrowed had to be repaid. I see nothing unbusinesslike in his choosing to repay those loans out

(1) 4 Tax Cas. 409, (1903) A. C. 129.

(2) 2 I. T. C. 139.

of capital rather than wait until he winds up his foreign business as the Commissioner of Income-tax suggests he should do.

Another argument addressed to us was that the remittances from the foreign business must be remittances of profits and not capital by reason of the fact that part of the sums remitted was used by the assessee for repaying the loans taken in Tinnevely for the conduct of the Tinnevely business and part for the personal expenses of the petitioner. With regard to the former reason, I think that the fact that the funds were utilised for repayment of the loans taken at Tinnevely supports the assessee's case rather than weakens it and with regard to the latter reason the use to which an assessee chooses to put his money on receipt of it cannot alter the character in which it was received. If this money was received in British India as capital, the fact that the assessee chose to use some of it for his own personal expenses did not change its nature.

For these reasons, the answer to questions (2) and (3) is that in the circumstances of this case the presumption as to foreign remittances being out of profits has been rebutted by the assessee.

Rs. 300 Costs of this reference are directed to be paid by the Commissioner of Income-tax to the assessee. Rs. 100 deposited is to be returned to the assessee.

RAMESAM, J.:—I concur with the order just pronounced by my Lord. On questions 2 and 3, I only wish to add that *Allan's* case(1) itself shows that the presumption laid down therein is a rebuttable presumption. To say that, even, where the party indicates on some evidence his wish to withdraw the capital, leaving the profits in the foreign country, he must be deemed to have withdrawn the profits and left the capital is to make the presumption irrebuttable. On the contention for the Income-tax Commissioner, (at one stage of the argument) the capital can only be brought up last *i.e.*, only when the trader wishes to wind up his business in the foreign country. This is to dictate to him in what order he should withdraw his funds and it is difficult to see why it should be so.

It must be remembered that this method of treating his funds is available to the party only once in respect of a particular item of capital. Only when another item of advance is made can he claim again to withdraw capital. If once it is conceded that the trader may call back his capital, it is for him to choose in what particular year he does so and to indicate his choice by accounts (which there is no reason to suspect) or otherwise. Once the choice is made, the presumption is rebutted.

KRISHNAN PANDALAI, J.:—I agree with my Lord for the reasons stated by him that it is not open to the assessee to raise before us the first question which relates to Rs. 43,810.

The 2nd and 3rd questions relate to Rs. 67,209 the amount which the Income-tax Commissioner attributed to foreign profits received in British India in the year of account and they both present different aspects of the same matter—whether the Commissioner was justified, on the account books and other materials furnished by the assessee and the nature of his business, in thinking that there was any presumption that the sum in question was profits and if there was any presumption in the matter, whether he ought not to have held that it was rebutted. Whether the sum was in fact profits or capital is ultimately one of fact.

But if in determining that fact, the Commissioner has acted on a presumption which either did not arise or which on the admitted facts must be held to have been rebutted, then the conclusion is vitiated by an error of law and this Court will correct it.

The ground of the Commissioner's decision is stated as follows in para. 5 of his order dated 3rd September 1927. "It is arguable that the appellant discharged debts due to creditors in British India, that he had no funds in British India to draw upon and he must therefore have drawn upon his foreign business. As there were profits in the foreign business more than sufficient to cover the discharge of these liabilities it must be presumed that these profits were drawn upon If the appellant incurred liabilities in the course of his British Indian business and met them by drawing on his funds abroad there is certainly a presumption that any profits that may have been available abroad were drawn on for this purpose." The Commissioner accordingly made a calculation based on a comparison of the volume of the Tinnevely business with that of the foreign business and computed Rs. 67,209 to be amount repaid on account of the purely British Indian liabilities and so held that sum to represent the foreign profits received at Tinnevely.

The question before the Commissioner was whether the balance according to the current account, as it is called, of remittances passing during the year between the Tinnevely head office and the foreign branches of the assessee's business represent or must be presumed to be profits. When regard is had to the nature of the assessee's business which may be broadly described as carrying on a money lending business in Travancore, and Cochin with money borrowed at Tinnevely, it is seen that the account is in no way intended to show the profits of the business at all but on the contrary it represents on one side the working capital sent by Tinnevely to the foreign shop and on the other, the amounts returned from the latter to Tinnevely for repayment to the depositors from whom the assessee had borrowed. There is a separate profit and loss account in the books of the foreign shops. There is no question that the books are not honestly and properly kept or that they were intended to conceal the facts. It was also admitted that if the opening balances in the account were taken into consideration there was no excess remittance to Tinnevely at all; the excess of Rs. 89,847 being the result if only the remittances during the year of account were taken. As to this the Commissioner in para 4 says "I think the appellant is right on this point also. The argument underlying what has been known as the 'theory of excess remittances' is that in so far as money brought into British India is found to be in excess of the sum required to replace money previously sent abroad, it should be presumed that the money sent in is a remittance of profit, if profit was available for remittance. In this case, there seems to be no doubt that the balance shown as due by the foreign shops at the beginning of the year represent money supplied at some time or other from Tinnevely. The 'net remittance' of Rs. 89,849 in the year of account was not sufficient to replace the sums supplied but not replaced in the previous years. A mere comparison of the amounts of remittances each way is not therefore by itself a sufficient ground for holding that money was sent in otherwise than by replacement of money previously sent out."

Having thus, I think rightly, held that a mere comparison of remittances each way is not sufficient to say that money was sent in otherwise than in replacement of money previously sent out, the Commissioner went on to hold, I think wrongly, that so much of the remittances to Tinnevely as were utilized to pay off Tinnevely debts must be presumed to be foreign profits received in British India.

It is difficult to see how the character of a remittance into British India, whether it is capital or profits, is to be judged by the use to which it is put after its receipt in British India. If a man received his foreign profits in British India, they will be equally liable to tax whether he pays debts, or gambles with them. But if what he received was not profits but his foreign capital he cannot be taxed here because he pays off therewith the debts he had incurred to carry on his business, local or foreign. The nature of the remittance must depend on what it was in origin. If the moneys remitted were not or cannot be presumed to be profits when remitted, the fact that debts were paid off with them cannot make them such.

Before us the main contention was not that the repayment of Tinnevely debts shows that the money with which it was done was from foreign profits brought into British India because it was recognised that it only showed that the assessee was paying off borrowed capital sent to foreign business and returned therefrom. But the main contention was that according to the rule in *Scottish Provident Institution v. Allan*(1) followed in *Murugappa Chettiar v. Commissioner of Income-tax, Madras*(2) when there are profits available in a foreign country and remittances are made from that country into British India the inference must be drawn that such remittances are from profits and this in spite of whatever the assessee may do and of the fact that according to the books of the assessee accepted as properly and honestly kept such remittances are shown to be and are honestly regarded by the assessee himself to be return of capital previously sent from British India to the foreign country for the business there.

The decisions cited do not support the contention to the length to which it goes. In the *Scottish Provident Institution* case about £1,500,000 had been sent to Australia for investment and after making the remittance in question there was still more than £1,800,000 in investment there. Apparently in order to escape the British tax, the Australian branch office of the company had according to instructions accompanied each of the disputed remittances with a letter to say that it was towards particular advances most of them made several years previously. On these facts the Lord President of the Court of Exchequer (Scotland) concluded his judgment in the lower Court with the observation that under the circumstances indefinite remittances to this Country must be presumed to consist of interest not of capital so long as the amount of capital remitted to Australia for investment still remains invested there. (4 Tax Cases 419) Lord Maclaren similarly said that the sound principle is that the source of the fund remitted in the absence of evidence to the contrary must be determined according to the ordinary course of business in dealing with un-invested funds (p. 420). In the House of Lords the Lord Chancellor referred to the instructions and letters above referred to as mere nicknaming the sum received and said that the right of the Crown could not be defeated thereby. (1903 A. C. 135) Lord Davey referred to the fact that the company had in all remitted 1½ millions to Australia and had at the end of the year in question 2½ millions there and that in every sense that is profit. As to the attempt to make out that what was remitted back were sums which had been sent out several years previously, his Lordship said it was mere book keeping and not actual facts. The mere calling it capital for the purpose of the Inland Revenue Department will not make into capital that which is essentially and in truth profit (p. 137). Lord Shand and Lord Robertson also referred to the fact that the sum still in Australia was more than the sum sent there (p. 136 and 138). The decision in *Murugappa Chettiar v. Commissioner of Income-tax, Madras*(2) does not carry the matter further than to show that where the Commissioner has not mis-directed himself as to the

(1) 4 Tax cas. 409

(3) 2 I. T. C. 139.

nature and scope of the presumption, the Court will not interfere with his inference on the question of fact whether the remittance was profits or capital.

In this case the Commissioner in my opinion misdirected himself in raising the presumption where the admitted facts did not leave any scope for it, or to put it in another way where he ought to have held that the admitted facts rebutted it. In the first place, the presumption is certainly rebuttable and can only be used in the absence of proof to the contrary. Whether the proof is sufficient is certainly a matter for the Commissioner only. But in the present case there is no dispute as to the facts *i.e.*, the course of business and assessee's books which are admitted to be honestly kept in the usual course of that business and the only question is what is the proper legal inference from those admitted facts and this is a question of law *Nofar Chandra Pal v. Shukur Sheikh* (1).

The Commissioner recognised that there was no ground in the amounts of remittances to and from Tinnevely for holding that more money was sent to Tinnevely than was necessary to replace capital previously sent out. He recognised that the foreign business was financed by borrowings at Tinnevely, and that these loans were repaid by remittances from foreign businesses. There was nothing to show as there was in the Scottish Provident Institution case that the investments still left in the foreign country were more or less than the unreturned capital plus the foreign profits earned more than three years prior to the year of account which are not liable to tax. The important fact on which the presumption was based in that case was therefore lacking in this and I am not sure that in using the presumption in that case care should not be taken to see that the circumstances are similar.

In any case, I cannot accede to the contention that even when it is shown that the assessee who has borrowed in British India and carried on a business with such borrowed capital and in foreign parts wants to return his borrowed capital and for that purpose remits that capital to British India and has deliberately and honestly maintained his books in the usual course to show what he has done, there is still a presumption that the source from whence he repays his debt is his foreign profits and not the borrowed capital. So long as it is open to a man to keep his foreign profits abroad, it is not for the Commissioner or any one else to compel him to do what he is not bound to do by law. After all a man can remit any particular amount of capital from foreign parts into British India only once and further remittances unless there were fresh capital sent out which could be returned must be from profits. The order in which a man must dispose of his capital and profits is for himself to determine and where as in this case, he has determined that order and there is nothing to suspect his *bona fides* or to show that his books are intended to conceal his real purpose, we cannot by resort to a presumption hold that he has done what he had not done and what he cannot be compelled to do.

I agree that the answer to the 2nd and 3rd questions must be as proposed by my Lord.

EDDY, J.:—I agree with the judgment of my Lord and desire to add only a word or two with regard to the construction of section 66 of the Indian Income-tax Act. The contention that under this section an assessee has alternative remedies is in my opinion untenable. It is quite plain from sub-section (2) of that section that an assessee who desires a question of law to be referred to the High Court must make his request to the Commissioner to refer it within

(1) I. L. R. 36 Cal. 189 at p. 195 P.C

one month of an order affecting him. *Expressio Unius Est Exclusio Alterius*. None the less it was contended before us that when he had allowed that time to go by he might avail himself of the provisions of the first sub-section of that section. The first sub-section of that section, in my opinion, confers no rights on the assessee at all. It is a provision, as I think, to enable the Commissioner to seek the assistance of the High Court when a question of law arises. Moreover the provision, as I think, contains its own time limit. Observe the words: "If, in the course of any assessment under this Act or any proceeding in connection therewith." If one reads these words in conjunction with the rest of the sub-section, it is clear, I think, that this provision is to enable the Commissioner to refer a question of law to this Court before he or any Income-tax authority subordinate to him, as the case may be, comes in the first instance to a final determination with regard to any assessment.

CORNISH, J.:—After the judgments which have been delivered it is hardly necessary to add anything more. But I will say a few words on the point raised in the argument whether the Court could entertain a question of law not referred to the Court by the Commissioner of Income-tax and which he had not refused to refer at the request of the assessee. The scheme of section 66 appears to be this: Sub-section (1) enables the Commissioner to obtain *suo motu* a determination by the High Court of a question of law. Sub-section (2) enables an assessee who has exhausted his right of appeal under section 32 to get a determination of a question of law by requiring the Commissioner to state a case and refer the question of law to the High Court; and sub-section (3) empowers the High Court to require the Commissioner to state a case if the High Court is satisfied, on the assessee's application, that the Commissioner should have referred the question of law which the assessee required him to refer. But clearly the time-limit imposed by sub-section (2) is intended to qualify the assessee's right to require the Commissioner to refer a question of law; and it seems to me equally clear from the language of sub-section (3) that the question of law which the Commissioner has refused to refer is the only question of law which the High Court can require him to refer on the assessee's application. The Commissioner cannot be called upon under sub-section (3) to state a case in respect of a question of law which the assessee has not required him to refer to the High Court under sub-section (2). If, therefore, the assessee fails to require the Commissioner to refer a particular question of law within the prescribed period of time he cannot after the expiry of that period apply to the High Court to call upon the Commissioner to refer it. Any other construction would, in my judgment, render the one month limit imposed by sub-section (2) meaningless. I agree with the proposed answers to the questions.

(355) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

*Before Mr. Justice Beasley, Chief Justice, Justice Sir V. Ramesam Kt.,
Mr. Justice Krishnan Pandalai, Mr. Justice Eddy and Mr. Justice Cornish.*

(20th January, 1930).

S. A. S. Subbiah Iyer

.. Assessee*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer

Indian Income-tax Act (XI of 1922), Sec. 4 (2)—Loan by money lending business outside British India—Debtor's properties in British India taken in

satisfaction of debt—Assessability as remittances of profit—Onus of establishing character of remittance.

Where the assessee carrying on a money lending business outside British India in satisfaction of a debt advanced there took the debtor's lands in British India, the lands so taken cannot be treated as a remittance in the shape of lands assessable under Sec. 4 (2) of the Income-tax Act, except as to interest earned by the loan within the period of three years prior to the account year.

The onus of showing that the remittances from a foreign business were from capital and not from profits and that they were from profits earned more than 3 years before the date of the remittances lies upon the assessee.

Case (O. P. No. 263 of 1928) stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras in compliance with the order of the High Court.

CASE.

In accordance with the High Court's order quoted above I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66 (3).

2. The petitioner is a resident of Tinnevely and carries on business in various places outside British India one of which is Quilon in the Travancore State.

3. The assessment now in question is that of 1927-28 and the year the profits of which are assessed to tax is the Malayalam year, Andu 1101 (year ending August, 1926). The Income-tax Officer found that in Andu 1101 the petitioner had received in British India a sum of Rs. 36,681 from his business at Quilon. This sum is made up as follows:—

	Rs.
Amount debited to the Profit and Loss account at Quilon and credited to the capital and drawing account in Tinnevely	25,000
Value of lands taken over in British India in partial discharge of loans due by debtors to the Quilon business (Rs. 7,029 and Rs. 3,845)	10,874
Value of articles purchased from out of the petitioner's Quilon profits and brought into British India ..	284
Money received from Quilon for payment of Income-tax ..	523

The Income-tax Officer worked out the profits of the Quilon business available for remittance to British India during the year of account to be Rs. 73,198 and

held that the sum of Rs. 36,681 received in British India was from such profits. He based his conclusion on the following figures.

Year of account.	Profits of year of account.	Amount available for remittance during year of account.		Remittances during year of account.	The year in which remittance was assessed.	Balance of unremitted profits at the end of year of account (Col. 3 minus Col. 4.)	
(1)	(2)	(3)		(4)	(5)	(6)	
	Rs.	Rs.		Rs.		Rs.	
1. Andu 1096	52,996	Not less than	52,996	17,359	1922-23	Not less than	35,637
2. „ 1097	56,560	Do do	92,197	11,470	1923-24	Do do	80,727
3. „ 1098	62,606	Do do	143,333	8,557	1924-25	Do do	139,776
4. „ 1099	45,978	Do do	185,754	12,152	1925-26	Do do	173,602
5. „ 1100	34,041	Do do	199,185	115,213	1926-27	Do do	83,972
6. „ 1101	10,774 (loss)		73,198				

The method of computation adopted by the Income-tax Officer was, in respect of each year, to ascertain the balance of un-remitted profits at the end of the preceding year and add to it the profits earned during the year in question. The total thus arrived at was taken to be the amount of profits available for remittance during that year, provided however that such total did not exceed the total of the profits of the year of account and of the three preceding years—See section 4 (2). If it exceeded the profits of these four years the excess was excluded and the total of the four years taken as the profits available for remittance. Thus, the profits available for remittance during the year of account, Andu 1100, which should otherwise have been Rs. 2,07,643 (Rs. 173,602 *plus* Rs. 34,041) was limited to Rs. 199,185 (the total profits for the four years 1097 to 1100).

The petitioner objected to the figure of Rs. 73,198 worked out by the Income-tax Officer. He contended that the profits received in British India in a particular year should first be presumed to have been remitted from the profits of that year and that if the money received be in excess of such profits, such excess should be presumed to have come out of the profits of the immediately preceding year and so on, and he claimed that if the assessments made in previous years were viewed in this light, the profits available in Andu 1101 and chargeable to income-tax under section 4 (2) would be only Rs. 929. He also claimed that two sums of Rs. 7,029 and Rs. 3,845 included in the figure of Rs. 36,681 being the value of certain lands taken over by him in British India in discharge of the debts due to his Quilon business, could not be held to have been received in British India and that in any case as the money was advanced to the debtors from his Quilon business on dates more than four years previous to the year of account the amounts could not be deemed to be profits falling within the period specified in section 4 (2). The Income-tax Officer rejected both the contentions and held (1) that the petitioner had not proved that the profits of the three years prior to the year of account had been received in British India in those years and assessed to tax and (2) that the money advanced to the debtors from the Quilon business of the petitioner was received by the petitioner only in the year in which the debtors paid it back and as the petitioner had obtained their lands in British India in lieu of cash during the year of account it was a

receipt during the year of account. A copy of the Income-tax Officer's order is filed marked Exhibit A.*

4. The petitioner appealed to the Assistant Commissioner but in respect of these points he met with no success. A copy of his order is filed marked Exhibit B.*

5. The petitioner then applied to me to refer two alleged questions of law to the High Court. I declined to refer them on the ground that the questions raised were not questions of law. A copy of my order is filed marked Exhibit C.*

6. On the petitioner moving the High Court under section 66 (3) the High Court has in its order quoted above directed me to refer the following two questions. The questions with my opinion thereon are as below:

Question 1: "Whether in the computation of foreign profits assessable under section 4 (2) of the Income-tax Act, there is any presumption in law available to the Income-tax authorities entitling them, in the absence of any specific facts or evidence, to appropriate the remittance of a sum of money as one made successively from out of the assessee's profits in the first, second or third year of the period of three years specified in the section and whether such allocation of the remittance to the earliest year of the said period based entirely on such a presumption of law is legal; or whether the remittance in any year should first be set against the profits of that year, the balance against the un-assessed profit of the immediately preceding year and so on."

A sum of Rs. 36,681 was received by the petitioner during the year of account and it is not disputed that it was remitted out of the profits of the Quilon business. Under the provisions of section 4 (2) it is therefore deemed to accrue or arise in British India. If the petitioner's case is that a portion of the profits received in British India really represented the profits that accrued or arose to him in his foreign business prior to the period of 4 years ending with the year of account, the burden of proving that fact, which is peculiarly within his knowledge, is on him. But he has not adduced any evidence on this point. He rests his case solely on a claim that there is a presumption in law that the remittances in a particular year represent the profits of that year. This question was the subject matter of the decision of the Madras High Court in *S. K. R. S. L. Firm v. Commissioner of Income-tax, Madras*, (1) and it was there held that there was no presumption either way and that the burden of proving the period in which the profits received by him in British India accrued or arose to him outside British India lay entirely on the assessee. The authorities below have found and I agree with their finding that the petitioner has not proved that the profits remitted during the year of account were sent out of the profits of any particular year. The question whether a remittance in a particular year was made out of the profits of that same year is a pure question of fact and I do not consider that there is any presumption in law that the remittance made in any year must be held to have come out of the profits of the same year.

Question (2): "Whether a purchase of lands in British India by the assessee carrying on a money lending business outside British India in satisfaction or part satisfaction of a loan advanced out of British India by the foreign business amounts to a receipt or bringing in of foreign profits into British India assessable under section 4 (2) of the Income-tax Act."

* Not printed.

(1) 2 I. T. C. 859.

The petitioner's suggestion seems to be that the lands are exhibited in the accounts as assets of the foreign business and that the purchase of the lands by the petitioner cannot be treated as a remittance. The position is that in satisfaction of certain debts due to his Quilon shop the petitioner (who is the sole proprietor of that business) took over the land of the debtors in British India. This means that Quilon money has come into his possession in British India in the shape of land and this can only be construed as a remittance. My opinion therefore is that the purchase of the lands in this case amounts to a remittance of profits and that it is taxable under section 4 (2) in the year in which the lands are purchased.

V. V. Srinivasa Ayyangar and P. R. Srinivasan, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

Two questions have been referred to the High Court, *viz.*,

- (1) Whether in the computation of foreign profits assessable under section 4 (2) of the Income-tax Act, there is any presumption in law available to the Income-tax authorities entitling them, in the absence of any specific facts or evidence, to appropriate the remittance of a sum of money as one made successively from out of the assessee's profits in the first, second or third year of the period of three years specified in the section and whether such allocation of the remittances to the earliest year of the said period based entirely on such a presumption of law is legal, or whether the remittance in any year should first be set against the profits of that year, the balance against the unassessed profit of the immediately preceding year and so on and
- (2) Whether a purchase of lands in British India by the assessee carrying on a money lending business outside British India in satisfaction or part satisfaction of a loan advanced out of British India by the foreign business amounts to a receipt or bringing in of foreign profits into British India assessable under section 4 (2) of the Income-tax Act.

Mr. Sreenivasa Ayyangar stated that he was not in a position to argue the first question because the remittances from Quilon to the assessee are not shown in the assessee's books to be remittances of capital. There were profits of a greater amount than the remittances from Tinnevely to Quilon earned in the Quilon business. The facts of this case are different to those in O. P. No. 180 of 1928 but the assessee is the same and in view of our observations during the course of the argument Mr. Sreenivasa Ayyangar has accepted the position that the burden of showing that the remittances were not from profits but from capital is upon him and that he is unable in this case to contend that he has discharged that burden. Here again we think that the question referred has not been properly framed and we content ourselves with saying that if there are profits in an assessee's foreign business sufficient to cover remittances to British India during the year of assessment the presumption is that the remittances were from profits and not from capital and that the onus of showing that they were from capital and not from profits lies upon an assessee and also the onus of showing that they were profits earned more than three years before the date of the remittance or remittances.

With regard to question (2), what happened was that the assessee in satisfaction of certain debts due to his Quilon shop took over lands of debtors in British India. The Income-tax Commissioner held that this money had

come into his possession in British India in the shape of land and could only be construed as a remittance. With this contention we do not agree. In one case a mortgage had been taken as security for a loan to a debtor and the mortgage was granted more than four years previous to the year of account. Clearly the interest received within the three years previous to the year of account and remitted to British India is assessable to income-tax. It is the profit earned by the loan and lending money is the assessee's business. The interest earned previous to the three years is not liable to income-tax at all and the repayment of the loan and its remittance to British India in that shape is a remittance of a repaid loan, namely, capital. Instead of remitting the repaid loan in the shape of money the assessee was forced to take in satisfaction of his debt instead of money the lands of his debtors in British India. In our view, by so doing he did not convert what, if it had been in the shape of cash, would have been a remittance from capital into a remittance of profits by taking lands in satisfaction instead of cash. The position is very different when an assessee invests profits made in the foreign business in lands or securities in British India. That is an investment of profits but that is not this case. If it can be shown that the foreign business has a debtor and that debtor is unable to repay the foreign business's debt and the assessee takes the debtor's land in British India in satisfaction of his claim against his debt the land so taken in British India is not taxable as foreign profits under section 4 (2) of the Income-tax Act and this answers the second question referred to us.

No costs allowed to either party. Refund of Rs. 50 deposit.

(556) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

Before Sir George Rankin, Kt., Chief Justice, Mr. Justice C. C. Ghose and Mr. Justice Buckland.

(27th January, 1930).

Messrs. Bisseswarlal Brijlal

.. Assesseees.

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer

Indian Income-tax Act (XI of 1922), Sec. 2 (14)—Registration of firm—Joint family business, conversion of, into partnership—Instrument executed by members as partners—Application for registration—Jurisdiction of Income-tax Officer to reject—Power to call for evidence.

Where an application for registration of a firm under section 2 (14) of the Income-tax Act was made accompanied by a document purporting to be the partnership deed executed among the members of a Hindu family in respect of the family business, and the Income-tax Officer in the absence of evidence which he required the assessee to produce showing the dissolution of the joint family rejected the application.

HELD, that the Income-tax Officer had power to call for evidence as to the reality of the instrument produced and to refuse registration in the absence of evidence properly required.

Case [Reference No. 4 of 1929] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal for the opinion of the High Court.

CASE.

Under the provisions of section 66 (2) of the Act I have the honour to refer the following case for the decision of the Hon'ble High Court.

2. Messrs. Bisseswarlal Brijlal, hereafter called the "Assesseees" a Hindu undivided family having their head office in Calcutta and a branch at Chakulia in the District of Singhbhum in Bihar and Orissa under the name and style of Surajmal Brijlal are dealers in piecegoods in Calcutta and owners of a rice mill and rice gola at the branch keeping the Ramnavami year ending usually in April as their year of account. They also possess house property and lease-hold property in Calcutta. On the 6th April, 1927 a notice under section 22 (2) of the Act was issued upon them calling for a return of their income during the previous year, viz., 1983 Ramnavami by 6th July 1927. They asked for time and time was granted till 12th October 1927. On that date they again asked for three months' time on the ground that the accounts had not been adjusted till then, their businesses at Calcutta and Chakulia having undergone a change in constitution, and put in an application for registration as a firm accompanied by a partnership deed, whereas previously they had always been assessed as a Hindu undivided family. They were informed by a post card notice that no further time would be given but actually no action was taken for another month. On the 14th November 1927 a notice under section 22 (4) was issued for production of accounts on the 19th November 1927 and in a separate letter they were asked to produce proof on the same date that the joint family had actually been dissolved. On the due date the accounts were not produced but a petition was filed asking for a further extension of time for production of accounts and submission of return till 20th December 1927 on the plea that as there was to be marriage in the family the accounts could not be adjusted. No proof was adduced to show that the Hindu undivided family had been dissolved, while in a subsequent application under section 27 they denied receipt of the Income-tax Officer's letter asking for such proof inspite of the fact that they actually received it which is proved by the signature of Bisseswarlal Brijlal on the acknowledgment slip brought back by the peon who served it. The same signature was given on the acknowledgment slip for the section 22 (4) notice the receipt of which is admitted. In the absence of any evidence the application for registration was refused. As no return was submitted the assessment was made on the 19th November 1927 under section 23 (4) for that default.

On the 14th December 1927 the assesseees presented a petition under section 27 on the ground that (1) they were unable to file the return as the accounts could not be adjusted, their business being a voluminous one, (2) the Income-tax Officer had no power to refuse registration (3) the whole income of the Chakulia business should not have been included in the assessment as it had become a partnership concern from the end of 1982. The Income-tax Officer rejected the petition under section 27 holding that (1) sufficient time had been granted for making the return, (2) the dissolution of the joint family was not proved and so the *bona-fides* of the partnership deed could not be tested, (3) there was a declaration by the Chakulia representative that Chakulia business was a branch of the Calcutta business. The decision of the Income-tax Officer was upheld by the Assistant Commissioner of Income-tax on appeal.

From the above account it is obvious that the assesseees had seven months' time from the date of service of notice under section 22 (2) till the date of assess-

ment in which to adjust the accounts and submit the return. The time should therefore have been ample and I hold that the Income-tax Officer showed them all reasonable consideration in the matter of allowing time and that the assessee's deliberately did not comply with the Income-tax Officer's requisitions.

As regards the refusal to register the newly constituted firm, in the absence of a return or accounts the Income-tax Officer had to satisfy himself that the deed of partnership had actually taken effect and was not a mere device to evade the proper payment of super-tax. He had some grounds for suspicion as the so-called partnership consisted of the former head of the family Bisseswarlal, his two sons and his two minor grand-sons represented by himself as their guardian. So the Income-tax Officer rightly asked the assessee's to prove the dissolution of the family, and I hold that the deed of partnership was certainly not a genuine document; for had it been so they would have come forward to prove its genuineness.

The business at Chakulia was admittedly a branch of the main business in earlier years. No mention of its having become a separate business was made till the 12th October 1927, when the 3 months' extension of time granted to the assessee's for filing a return expired. If the plea had been a genuine one surely they would have mentioned the fact when they applied for time first i.e., in July. Further more, when the Income-tax Officer, Singbhum, called on the Manager of the business there by a notice under section 22 (2) to submit a return of income he replied that the firm always paid tax at Calcutta, where the head office was, and that he had no accounts there. This was on the 21st May 1927. It is thus clear enough that the Chakulia business was a branch of the main business on that date. The date in question was quoted in the appellate order as 21st March 1927, by mistake. The Income-tax Officer has therefore rightly included the whole income of the Chakulia branch in the assessment.

The assessee's have now asked, in the event of my declining to interfere in revision under section 33, for a reference to the High Court of the following questions of law:

- (i) Whether the Income-tax Officer has any power under the law to refuse an application for registration made in the prescribed manner with partnership deed prior to assessment and if so, under what section of the Act?
- (ii) Whether or not an agreement of partnership executed by and between the male members of a Mitakshara Hindu family for dividing the capital and profit and loss in accordance with defined shares being acted upon extinguishes the essential incidents of jointness, namely, commensality of interest and survivorship and dissolves the family?
- (iii) Whether the law gives the Income-tax Officer any power to call for evidence of dissolution of the joint family for the purpose of registration under section 2 (14) over and above the documentary evidence adduced by the partnership deed in support of the application in Form I under Rule 2.
- (iv) Whether a report from a District Income-tax Officer in respect of the constitution or income of an alleged branch is legal or not in the absence of any notice under section 22 (2) or 22 (4) issued and served by that District Income-tax Officer on the branch concerned.

- (v) Whether the report of a District Income-tax Officer regarding the constitution and income of an alleged branch based upon an enquiry in respect of a prior year's assessment can in law override an assessee's contention before the assessing Income-tax Officer in respect of the subsequent year's assessment of the firm with a different constitution under contract?

I have declined to interfere in revision. As regards the 5 questions of law which I am asked to refer to the High Court I am of opinion that question 2 does not arise as it is clear enough that the partnership deed had not been acted upon at the time the assessment was made. On that date the accounts of the business had admittedly not been adjusted and no allocation of income had been made between the partners. In other words clause 9 of this partnership deed had not been put into effect.

Question 4 contains a misstatement of fact as the Income-tax Officer, Singbhum's report shows that notice under section 22 (2) was served on the assessee.

Question 5 does not arise as the Income-tax Officer, Singbhum's enquiry was not in respect of a prior year's assessment as his report shows but had to do with the accounting year in question.

I am unable therefore to refer any of these 3 questions to the High Court.

Questions I and III actually arise in this case and I therefore refer them with my opinion which is as follows.

These two questions are dealt with together. The Act itself says nothing about the method of registering a firm. How this is to be done is described in rules 2 to 6. Now it is true that the rules do not give the Income-tax Officer any definite power to reject an application for registration, but it must be assumed that the Income-tax Officer has the power inherent in all registering authorities to reject an application whose *bona-fides* he has good reason to suspect. In the present instance the registering of the firm was certain to alter the method of assessment very materially from that followed in previous years, and it was important that the Income-tax Officer should know whether the changed constitution of the firm had actually taken effect. Now at the time the application for registration of the firm was made, some six months after the expiry of the accounting year, no return had been filed. The assessee's excuse was that the accounts had not been adjusted, and this although clause 9 of the partnership deed provides that the accounts should be taken and adjusted at Ramnavami time (the close of the assessee's accounting year) every year. It was therefore certain that the profits had neither been ascertained nor allocated amongst the partners. The Income-tax Officer then called for accounts both for assessment purposes and to see if the deed had been acted upon, but these were not produced.

It seems to me that the Income-tax Officer had in the circumstances every reason to suspect the *bona fides* of the application for registration especially as the registering of the firm was likely to save the partners from the payment of a considerable sum in super-tax. He was therefore justified in calling upon the assessee to produce some other proof besides the accounts that the partnership deed had been acted upon. His order took the form of a letter calling upon the assessee to adduce proof that the Hindu undivided family had been dissolved. No evidence was adduced and the flimsy excuse was subsequently made that they had not received his letter, though the signature of Bisseswarlal Brijlal is on the receipt brought back by the peon who delivered it.

JUDGMENT.

RANKIN, C. J.:—In this case, the Commissioner of Income-tax, Bengal, has referred to this Court under section 66 (2) of the Indian Income-tax Act of 1922 two questions: (1) Whether the Income-tax Officer has any power under the law to refuse an application for registration made in the prescribed manner with partnership deed prior to assessment and, if so, under what section of the Act and (2) Whether the law gives the Income-tax Officer any power to call for evidence of dissolution of the joint family for the purpose of registration under section 2 (14) over and above the documentary evidence adduced by the partnership deed in support of the application in Form I under Rule 2.

Now, it is abundantly clear that the assesseees in this case carry on a certain business. The Income-tax Officer says that this business has been assessed on the footing that the persons who carry it on are members of a Hindu undivided family in business as such. It seems there is the grand-father who is the senior member and there are grand-sons who are minors; and the business has been treated in that way until the time with which we are now concerned.

It appears that, after notice requiring a return of income for the year 1927-28 had been issued, the assesseees, on the 12th October 1927, applied, purporting to make the application under the Rules laid down in the Income-tax Manual, for registration of the firm as a registered firm within the meaning of clause (14) of section 2 of the Act. They produced a document according to which these various members who had formerly been assessed as a Hindu family said that the parties had been carrying on the business for a long time and that "for various reasons it has become necessary that their respective shares should be defined." Then the document purported to describe an ordinary contractual partnership—each one of the five members of the firm including the minors being stated to have an one-fifth share. On this document being presented to the Income-tax Officer, he was immediately suspicious of it because it appeared to him that, while no doubt the members of an undivided Hindu family owning a family business might dissolve the family business and enter into a contractual partnership business on their own account, the probabilities of that having been done in the circumstances of this case were extremely remote. It seems tolerably clear in the absence of some evidence to the contrary, that this piece of paper which the parties had signed was expected to be magical talisman which would protect them from the imposition of super-tax and had no other reality at all. In these circumstances, the Income-tax Officer required the assesseees to produce evidence of the *bona fides* of this document—some evidence to show that the family as a family had been dissolved, some evidence to show that the business which had formerly been treated as a joint family business had really and, in fact, ceased to be so; and no such evidence was forthcoming.

The question which the Income-tax Officer was asked to refer to us was whether any set of people purporting to be a firm as described by clause (14) of section 2 were not entitled to get themselves registered as a registered firm under the Rules, however much the document upon which they relied was either forged on the one hand, or intended not to be acted upon, or otherwise a pure unreality. It is said that the Rules contain no provision for an investigation into the reality of such a document. Neither they do. On the other hand, under the Act and under the Rules, the right to present such a document at all is only given to a firm constituted under an instrument of partnership specifying the individual shares of the partners; and, if a firm is not a firm in fact constituted under such an instrument of partnership, the Income-tax Officer, in my judgment, is not obliged to receive the application at all, or to register the document which the parties were putting forward. It may or may not be, in view of the meti-

culous character of some of the other provisions of the Act, that it would be as well to prescribe expressly that the Income-tax Officer may investigate such a question as the present. But there is nothing in the Act to show that he may not investigate such a question and I dissent from the doctrine that before investigating into anything the Income-tax Officer has to show that his investigation is required or permitted by the express terms of a section. In the present case, a duty is cast upon him by clause (14) of section 2 and by the Rules made thereunder, and in order to work the Act properly, it appears to me that he has power to call for evidence as to the reality of the instrument produced.

In these circumstances, it would be sufficient to answer the first question by saying that the Income-tax Officer has the power referred to. As regards the third question, the answer should be in the affirmative.

The assessees must pay the costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree and desire to add only a few observations. The first question stated broadly appears to be whether the Income-tax Officer has power to enquire whether a person or a body of persons is or are what he or they represent themselves to be for the purpose of taking advantage of a provision of the Act. If the question is so stated, it becomes clear that the Income-tax Officer must have power to make the enquiries necessary to satisfy himself as to the person or persons with whom he is asked to deal. If the reply to the first question propounded is in the affirmative, it would, in my opinion, be a sufficient reply to the third question to say that the Income-tax Officer is entitled, for the purposes of such enquiries as the reply to the first question contemplates may be necessary, to call for any evidence which may properly be required. Speaking for myself, it may be that in this particular matter the Income-tax Officer was right in calling for evidence of dissolution of the joint family, and it certainly cannot be said that he was not. But I prefer to base myself on more general grounds and to say that when persons claim to constitute a partnership firm for the registration of which they make an application the Income-tax Officer may call upon them to prove by evidence that they are what they claim to be before he proceeds further with the application.

(557) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin Kt., Chief Justice, Mr. Justice Ghose and
Mr. Justice Buckland.*

(27th January, 1930).

N. S. Mundy

.. Assessee.*

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer

Indian Income-tax Act (XI of 1922), Sec. 4—Employee claiming share as partner—Money received in satisfaction of the claim—If assessable.

Where the assessee employed as the Manager of a business remunerated by a share of profits claimed a quarter share in the business as partner on the basis

* A. I. R. (1930) Cal. 625 ; 34 C. W. N. 788.

of an alleged agreement by the owner of the business and received a sum of Rs. 60,000 in satisfaction of the claim,

HELD, that the sum of money so received was not "income, profits or gains" within the meaning of section 4 of the Income-tax Act.

Turner Morrison and Co., Ltd. v. Commissioner of Income-tax, Bengal, 3 I. T. C. 219, *Distinguished*.

Case [Reference No. 12 of 1929] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Assam for the opinion of the High Court.

CASE.

I have the honour to forward herewith under section 66 (2) of the Indian Income-tax Act, XI of 1922, a statement of facts for the opinion of the Hon'ble High Court. The reference is made on the application of Mr. N. S. Mundy of Silchar.

2. The applicant Mr. N. S. Mundy was from 1906 to 1926 the Manager in Silchar of a business known as Messrs. John Smeal and Company, which was owned by Mr. J. W. Trotman. The conditions of Mr. Mundy's employment varied from time to time, but for some years prior to 1924 he was in receipt of pay at the rate of Rs. 600 a month and was further entitled to commission at 25 per cent. of the nett profits each year when accounts were finally made up.

3. In May 1924 Mr. Trotman having returned to India, wrote to Mr. Mundy a letter on a paper stamped with eight annas a copy of which is attached to this case.* In this letter he states "your position has been and remains virtually that of a quarter shareholder in the business." He announced his intention of converting the business into a limited liability company of which one quarter of the shares would be allotted to Mr. Mundy. It is a reasonable deduction, that the shares would be allotted as fully paid up without a cash payment, in return for the services of Mr. Mundy in extending and improving the business of the firm.

4. During the course of 1925 differences arose between Messrs. Trotman and Mundy and after certain correspondence, copies of which are attached hereto, it was agreed that Mr. Trotman should pay Mr. Mundy Rs. 60,000, whereupon Mr. Mundy should cease connection with the business. In April 1926 the sum of Rs. 55,000 was accordingly paid to Mr. Mundy who gave a receipt for Rs. 60,000 "as a full settlement of my claim to a partnership in the firm of John Smeal and Company, Silchar."

5. The receipt of this money was not entered by Mr. Mundy in his income-tax return in 1927-28 and the sum was not assessed in that year. In 1928-29 the payment came to the knowledge of the Income-tax authorities, who acting under section 34 of the Act made a supplementary assessment on Mr. Mundy. Against this supplementary assessment Mr. Mundy appealed to the Deputy Commissioner, Cachar, as Assistant Commissioner of Income-tax; the appeal was rejected, the judgment being attached herewith as Appendix No. 3.* Mr. Mundy now applies for a revision of the assessment or for a reference to the High Court. I am not prepared to revise the order and accordingly submit to the High Court the question put in detail below in paragraph 8.

* Not printed.

6. The following additional facts are admitted or proved:—

- (a) Mr. Mundy at no time contributed in cash to the capital of the business.
- (b) Mr. Mundy at no time did any acts by way of management of the business which indicated a claim of power to bind the firm, beyond the powers given him by a power of attorney from Mr. Trotman.
- (c) The question of liability for losses was never raised, the business having all along been prosperous.
- (d) There are two civil suits now pending before the Sub-Judge at Silchar, between Mr. Mundy and Mr. Trotman, in one of which the following issue has been framed:—“Did the plaintiff (Mr. Mundy) become partner with the defendant from April 1924.” This suit is not likely to be decided for a long time.
- (e) In the income-tax returns of Messrs. John Smeal and Company the pay and commission of Mr. Mundy have always been deducted; this would not be allowable if Mr. Mundy had been a partner.

7. The questions to be submitted to the High Court are not framed by the applicant. His first ground is limitation, but on this he is clearly wrong, and no question of law arises for submission. The money was received in April 1926, and should have been assessed in 1927-28. It “escaped assessment” in that year within the meaning of section 34 and was therefore rightly assessed in 1928-29.

8. The other question which emerges from the grounds stated in the application may be stated as follows:—“Was the Income-tax Officer correct in holding that the applicant’s interest in the business did not amount to a partnership, or to such an interest as would entitle the Income-tax department to regard money received in exchange for it as a capital receipt, and not income?”

9. I am required to state my opinion on the point submitted. I am clearly of opinion that no partnership ever came into existence. Mr. Trotman’s letter of 21st May 1924 can, put at the highest, only amount to an agreement that if the business be converted into a limited company Mr. Mundy would be allotted one quarter of the shares. Possibly the agreement might have been enforceable; but when the offer was definitely made in Mr. Trotman’s letter of 12th March 1926 it was rejected by Mr. Mundy *vide* his letter of the 15th March, and we are accordingly thrown back on the “virtual” partnership of the letter of May 21st, 1924. In my opinion this does not constitute a saleable interest; and the payment by Mr. Trotman was an *ex gratia* payment to Mr. Mundy in consideration of the fact that the latter had served him long and well. The payment, though a single one, arose out of Mr. Mundy’s profession, vocation or occupation within the meaning of section 4 (3) (vii) of the Act and is therefore liable to the payment of income-tax.

JUDGMENT.

RANKIN, C. J.:—This is a reference by the Commissioner of Income-tax, Assam, and the question arises whether or not a certain sum amounting to Rs. 55,000 paid in April 1926 by a Mr. Trotman to the assessee is liable to income-tax.

It appears that Mr. Trotman in 1924 was the owner of a business which he carried on under the style of John Smeal and Co., Mr. Mundy the assessee, was engaged by Mr. Trotman as an assistant in the business. It may be that the word "assistant" is not a quite sufficient description and that Mr. Mundy might be described as Manager; but Mr. Mundy began as a servant of Mr. Trotman and he had to begin with no interest save that of an employee in his master's business. It appears that, by the 21st May 1924, Mr. Mundy had been serving his employer so well that for a good many years past it had been understood between them that, although there was no formal partnership, he had the position which Mr. Trotman described as "virtually that of a quarter share-holder in the business." The reason of this was that Mr. Mundy was being remunerated, it would seem, by 25 per cent. of the profits, and Mr. Trotman held out to Mr. Mundy that he was going to make a will, that he wished to convert the business into a limited liability company and to give Mr. Mundy a share. As to his intention to give Mr. Mundy this interest in this way, there is evidence of a letter of the 21st May 1924, Trotman saying that he is putting his intention into writing so that Mundy might have a tangible guarantee of his position. Later on, it appears that Mr. Mundy was taking up the position that he had been given a right to a quarter interest in the capital of this business, that he was a partner, or at the worst was a person who had an enforceable agreement with Trotman to give him the interest of a partner to the extent of one-fourth share. Trotman was taking up the attitude "you are not a partner in fact. It is true that I did promise that I was going to convert the business into a limited company and give you a quarter of the shares. That has not been done and you Mundy are not desirous any longer that I should do so." Mundy was maintaining that he had an even higher right, namely, a right to a quarter interest in the business apart from any question of a limited company. In that position, Mundy made an offer to Trotman that he was willing to take Rs. 70,000 for his quarter share of the business and there is no doubt, on the terms of the letter, that he was claiming it not as an *ex gratia* payment but as a sum of money which he would take in lieu of what he alleged to be his right. Now Trotman in reply did not admit that Mundy had the right he claimed but he said that just as he was willing to convert the business into a limited company and give Mundy one quarter of the shares, so in lieu of that he was willing to let Mundy have Rs. 60,000 i.e., to give in cash what he had expressed willingness to give in kind. This offer was accepted in a letter in which Mundy said "I am willing to accept your offer of Rs. 60,000 in payment of my quarter share of the business."

Now, the Commissioner of Income-tax, Assam, was, in the first instance, the authority to find upon all necessary questions of fact. It is quite true that he has found that Mr. Trotman's letters only amounted to an agreement that, if the business was converted into a limited company, Mundy would have a quarter of the shares. He says: The agreement might have been enforceable but as Mundy did not in the end accept the offer of a quarter share in the company that matter ended there. Accordingly, says the Income-tax Commissioner, there is no partnership proved; we are thrown back on the letter in which Trotman speaks of Mundy as having the position virtually of a quarter share-holder in the business. Thereupon, the Income-tax Commissioner goes on to say "In my opinion, this does not constitute a saleable interest; and the payment by Mr. Trotman was *ex gratia* payment to Mr. Mundy in consideration of the fact that the latter had served him long and well."

Now, in my judgment, the Income-tax Commissioner misdirected himself in law in holding that, upon these findings of fact, this payment was for tax purposes to be regarded solely as an *ex gratia* payment to Mr. Mundy in considera-

tion of the fact that the latter had served him long and well. It may be quite true that Mr. Mundy had no right of a partner; but he certainly was claiming to have that right and he was claiming upon grounds which, as far as I can see, may well have had some foundation. The letter accepting Rs. 60,000 was a letter accepting it "in payment of my quarter share of the business." We have to look at this sum and determine the nature and character of the receipt from Mr. Mundy's point of view. He, not Mr. Trotman, is the assessee. How and for what did Mundy receive or acquire the money? He got it by pressing and then compromising a claim to a partnership which claim was no doubt fairly formidable, for the sum of Rs. 60,000 would not have been given in exchange therefor. It seems to me that the Income-tax Commissioner thought himself obliged on the correspondence to hold this to be an *ex gratia* payment in consideration of the fact that Mr. Mundy had served Mr. Trotman long and well, merely because he could not find that, in point of fact, there was a right of a partner in Mr. Mundy. In so doing, I think the Income-tax Commissioner has misdirected himself and I am clear that, on this correspondence alone Mr. Mundy took this money in satisfaction of his claim to be entitled to a quarter share in the business. It seems that there was a suit between the parties in which an issue was framed "Did the plaintiff Mundy become partner with the defendant from April 1924."

Now, this payment of Rs. 60,000 was in settlement of Mundy's claim. That being so, it appears to me that we have to consider whether such a payment is "income, profits or gains" at all within the meaning of the Indian Income-tax Act. If a man claims an interest in the capital of a business and in the end receives Rs. 60,000 in satisfaction of all claims he may have in the capital of the business, is that income liable to income-tax? In my opinion, it is not liable to income-tax and for the same reason that withdrawal of capital from a firm would not be liable to income-tax. We have not had the matter argued by learned counsel for the assessee at any length; but I may say that, if the assessee's case had depended upon his showing that the payment was within clause (vii) of sub-section (3) of section 4, as at present advised, I should have thought that the payment being one arising out of business that clause did not apply. I am of opinion that the sum of money here concerned is not "income, profits or gains" within the meaning of section 4 at all.

A recent case in *Turner Morrison and Co., Ltd. v. Commissioner of Income-tax, Bengal*(1) has been cited to us on behalf of the Commissioner of Income-tax. That case appears to have been decided under clause (vii) of sub-section (3) of section 4 and other arguments appear to have been addressed to the Court upon the question whether the sum of money there fell within section 10, or section 12 of the Income-tax Act. I do not observe that the case was argued upon the footing that the payment in that case was of a character such as would prevent it from being "income, profits or gains" at all within the meaning of the Income-tax Act. I think the special circumstances of that case probably account for the fact that this aspect of the question was not dealt with in the judgment. It appears from the terms of the Articles of Association of the Company that the Managing Agents had to take whatever remuneration the Company would agree to in its annual meeting. In the course of a year the Company went into voluntary liquidation and, in these circumstances, assuming that there was no other reason why the Managing Agents should not make a claim for wrongful dismissal, it is obvious that they would have some difficulty in recovering much by way of damages for wrongful dismissal if their remuneration after doing the work was entirely in the hands of their employers. It would seem that, as the Company was being wound up, a large sum of money was paid to the Managing Agents—a

sum considerably in excess even of the remuneration which had been paid for a whole year in either of the preceding years; and, in these circumstances, it is perhaps not altogether to be wondered at that the sum of money (in that case was dealt with as a question of *ex gratia* payment made to the Managing Agents in consideration of the fact that they were losing their expectation of continuing to do business as the Managing Agents of the Company. In any case, that matter is not on all fours with the question with which we are here concerned. If I am right in thinking, upon the correspondence in the present case that Rs. 60,000 was paid and received in satisfaction of a *bona fide* claim on the part of the assessee to be entitled to an interest in the capital of a certain business, it does not seem to me that that is liable to income-tax.

Accordingly, the question propounded to us should, in my opinion, be answered in favour of the assessee. The question is not perhaps very happily worded—"Was the Income-tax Officer correct in holding that the applicant's interest in the business did not amount to a partnership or to such an interest as would entitle the Income-tax Department to regard money received in exchange for it as a capital receipt and not income." In my judgment, as to the latter part of that question, the Income-tax Officer was not correct. Whether Mr. Mundy had or had not a right to a quarter interest in this business, if he received the Rs. 60,000 in satisfaction of a *bona fide* claim that he was entitled to a quarter interest in the capital, the money so received is not taxable.

The assessee will have his costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(558) IN THE COURT OF THE JUDICIAL COMMISSIONER, NAGPUR.

*Before Mr. Findlay, Judicial Commissioner and Mr. Macnair, Additional
Judicial Commissioner.*

(29th January, 1930).

Seth Sheolal Ramlal

.. Assessee

v.

The Commissioner of Income-tax, Central Provinces
and Berar

.. Referring Officer.

*Indian Income-tax Act (XI of 1922), Sec. 2 (1) (b)—Ginning Cotton—
Sale of ginned cotton, profits therefrom—If agricultural income—If process
essential for marketing.*

*Profits made by an assessee by selling ginned cotton instead of selling it
unginned as grown by him is not agricultural income within the meaning of
Sec. 2 (1) (b) (ii) of the Income-tax Act.*

*Ginning cotton is not a process ordinarily employed by cotton cultivators
to render it fit to be taken to the market.*

Case [Miscellaneous Judicial Case No. 20 of 1929], stated under Sec. 66
(2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-
tax, Central Provinces and Berar for the opinion of the High Court.

CASE.

Seth Sheolal Ramlal, calling himself a banker, and residing at Mohogaon in the Chhindwara district, had returned an income of Rs. 17,819-11-6 for assessment during the year 1928-29. The Income-tax Officer looked into his accounts and calculated his taxable income at Rs. 24,618 which he taxed. In arriving at this income, among other items, the Income-tax Officer disallowed bad debts amounting to Rs. 186-3-6 calling them "time barred long before the account year." He also calculated an income of Rs. 1,010 on the cotton grown by the assessee in his own villages and ginned by him in the New Mofussil Ginning Factory at Pandharkeoda, another village in the same district and sold in the markets of Bombay. The Income-tax Officer also found that an income of Rs. 450 was concealed by the assessee and therefore under section 28 of the Income-tax Act levied a penalty of Rs. 28 on account of this concealment.

2. Against this assessment two appeals were filed. One was against the order under section 28 and the other against the order under section 23 (3), i.e., as regards bad debts being disallowed and the income of Rs. 1,010 from cotton business being added. The first appeal succeeded and the penalty was remitted; but the second appeal failed on both points. The result was that the assessment stood on the original figure.

3. The assessee has now put in an application under section 66 (2) (copy enclosed)* in which he requests that the following two points arising out of the facts of the case be referred to the High Court:—(i) Whether the Income-tax Officer is entitled to calculate profits on the cotton which is the agricultural produce of the assessee's own villages simply because he gets it ginned in the ginning factory before he takes it to market for sale and assess tax on such profits under the Indian Income-tax Act. (ii) Whether the assessee is not entitled to the deduction of any amount which he had written off as bad debts in the account year if the amount became time-barred in the previous year.

FACTS. 4. Point (i). The assessee owns 20 villages in the Chhindwara District. He has some home-farm cultivation also and along with some grains, grows cotton in 13 of his villages. He has no ginning or pressing factory of his own. In the account year he grew 186 Khandis and 4 maunds of cotton in his villages, took all this cotton to Pandharkeoda, another village in the district, where there are ginning and pressing factories and got it ginned and pressed in the New Mofussil Company Ginning Press, and converted it into 101 bales of cotton which he despatched to Bombay and sold in the market thereof for Rs. 21,613-3-0, and took the whole of this income to his agricultural accounts. The Income-tax Officer while examining the accounts found this out and asked the assessee to give him the market value of the *Kapas* (unginned cotton) on the date on which it was ginned so that, after taking into account the price of the cotton and the expenses of ginning and pressing it and the railway freight to Bombay, he could find out the extra income made by the assessee on this business. The assessee refused to give this information and the Income-tax Officer was compelled to take Rs. 10 per bale as the extra income made by the assessee, i.e., the income made by him after the process of manufacture had been completed and thus calculated the total income from this business to be Rs. 1,010.

OPINION. 5. The assessee contends "that with the development of the machinery and the scarcity of labour, the ginning of agricultural cotton is now the process ordinarily employed by the petitioner and several big *Malguzars* in

the cotton districts to render the agricultural cotton fit to be taken to market and as such he should not have been charged with the profits on the sale of such cotton and the levy of tax on Rs. 1,010 is simply wrong." He thus seems to rely upon section 4 of the Income-tax Act which exempts "Agricultural income" from taxation and upon section 2 (1) (b) (ii) which defines "agricultural income." In the first place it is not a fact that the ginning of agricultural cotton is now the process ordinarily employed by growers of cotton to render it fit to be taken to market. In the statement made before me, even the assessee has himself admitted that many carts of cotton are brought by cotton growers to even Pandharkeoda, where there are three ginning and pressing factories, and where this cotton in raw state is purchased by several companies and other traders. It is not so only at Pandharkeoda. But it is within the common knowledge of all in all places including Berar where cotton is grown on a large scale that the growers of cotton still sell it in the raw state and that it is mostly the traders including big companies who purchase it, and then gin it and press it and then send it to Bombay for sale in the market thereof. My finding on the question of fact, therefore, is that cotton "is ordinarily sold in the market in its raw state", i.e., as *Kapas* and the application of machinery to gin it and to sell it in Bombay was not the ordinary process but was, as admitted by the assessee, resorted to with the object of making greater profit. This extra profit seems to have been therefore correctly assessed [*The Killing Valley Company, Ltd. v. The Secretary of State for India*, (1) and *In the matter of Bikanpur Sugar concern*, (2)]. I would submit that this question be answered in the affirmative.

6. *Point (ii).*—As the amount of the bad debts disallowed is very small and as the Department has already put in an application to this Honourable Court for appeal to the Privy Council in another important case on the same point, I, under the powers given to me by section 33 of the Income-tax Act, have, for the time being, allowed this to be deducted from the total taxable income. Reference on this point is therefore not made.

M. B. Kinkhede, and V. R. Dhoke, for the Assessee.

D. N. Choudhri, for the Crown.

JUDGMENT.

This is a reference by the Commissioner of Income-tax, Central Provinces and Berar, under section 66 (2) of the Indian Income-tax Act of 1922. The applicant, Seth Sheolal Ramlal, Banker, owns various villages in the Chhindwara District. Amongst his crops he grows cotton and it is apparently his practice, instead of selling the cotton in a crude state, to send it to a ginning factory at Pandharkeoda, another village in the same District. Having had the cotton ginned there, he sells it in Bombay at a price naturally much higher than he would have obtained if he had sold the crude produce in its original state. The Commissioner of Income-tax accordingly assessed him on a profit of Rs. 1,010 assumed to have been made in this way, and thus the following question has been referred to us for decision:—"Whether the Income-tax Officer is entitled to calculate profits on the cotton which is the agricultural produce of the assessee's own villages simply because he gets it ginned in the ginning factory before he takes it to market for sale and assess tax on such profits under the Indian Income-tax Act."

2. On behalf of the applicant it has been urged before us that it is in every way an advantageous matter to have the raw cotton ginned straightway;

when the cotton seed has been extracted, the danger of fire is much lessened, much space is saved and a great reduction in transport charges occurs. Section 2, sub-section (1) (b) (ii) of the Income-tax Act lays down that agricultural income will also include "any income derived from land by the performance by a cultivator of any process ordinarily employed by a cultivator to render the produce raised or received by him fit to be taken to market." It has been suggested on behalf of the applicant that, even assuming that it is not the general practice amongst the cultivators to have their cotton ginned in the first instance, as he does, the sub-section quoted should be taken as implying that the process in question should be postulated to be one "ordinarily employed by an agriculturist" in the position and standing of the applicant. We do not think, however, that this interpretation is the correct one. The process "ordinarily employed by a cultivator" must, in our opinion, mean one in ordinary use amongst cultivators generally, and the Income-tax Act, so far as agricultural income is concerned, only relieves the producer from liability to income-tax so long as he is a *bona-fide* agriculturist carrying on that business in the ordinary course of good husbandry. Again, although it may be distinctly advantageous, even from the mere point of view of transport to have the cotton ginned first, we are not prepared to hold that this process was essential in order to enable the produce to be "fit to be taken to market." Any such interpretation would, in our opinion, involve an undue straining of the sub-section quoted above.

3. It is not disputed that the applicant did obtain a profit of Rs. 1,010 by adopting the course he did adopt instead of selling the unginned cotton. The Commissioner of Income-tax has given a definite finding that the ginning of agricultural cotton is not at present the process ordinarily employed by growers of cotton to render it fit to be taken to the market. We cannot go behind that finding of fact which was, as a matter of fact, largely based on an admission made by the assessee himself. On the question of law we have held that the Commissioner's interpretation of section 2, sub-section (1) (b) (ii) of the Income-tax Act is correct.

4. We are of opinion, therefore, that the position of the applicant cannot be upheld and we, therefore, answer the question referred to us in the affirmative. The applicant must bear the costs of the Commissioner of Income-tax. We fix these at Rs. 75.

[359] *PRIVY COUNCIL.*

ON APPEAL FROM THE HIGH COURT OF JUDICATURE AT BOMBAY.

Present.—*Lord Blanesburgh, Lord Warrington of Clyffe and Sir Charles Sargant.*
(30th January, 1930).

The Trustees Corporation (India) Limited

.. *Appellants.* *

v.

The Commissioner of Income-tax, Bombay

.. *Respondent.*

Income-tax Act (XI of 1922), Secs. 4, 10, 24 (1) and 66—Indian Company incorporated for dealing in shares—Agreement to purchase Burma Corporation shares—Price not paid in cash but in allotment of shares in Vendee Company—Substantial difference between market value of shares purchased and face value of shares allotted—Burma shares not delivered to Vendee Company but resold by

* L. R. 57 I. A. 152; I. L. R. 54 Bom. 437; 59 M. L. J. 242, A. I. R. (1930) P. C. 151.

Vendors—Sale proceeds less than the face value of allotted shares—Deficiency claimed as a trading loss by Indian Company—Indian Company if entitled to take face value of its shares as purchase price of Burma shares—Scope of Sec. 66.

The Appellant, an Indian Company promoted on the 10th February, 1920 by two English private Companies, on the same date entered into an agreement with the latter for the purchase of a large block of shares held by them in Burma Corporation, Ltd., in consideration of allotting to the vendors an equal number of its own shares of the face value of Rs. 200 and in pursuance thereof allotted to them a moiety of the shares to be so allotted. The English Companies never handed any of the Burma shares to the Appellant within the period of 3 years fixed for delivery and on the 14th November, 1923 entered into a supplementary agreement *inter alia* providing for extension of time for delivery by three more years, remitting the allotment of the other moiety of the shares and giving them power to sell the shares with the Appellant's consent; the sale proceeds together with dividends to be paid over to the Appellant. In January, 1924 the Burma shares were accordingly sold in London by the English Companies at a price of Rs. 168 per share, the sale proceeds being kept by them as a deposit by the Appellant.

On an assessment to super-tax in respect of the dividends from Burma shares and interest amounting to over 20 lakhs, the Appellant claimed to set off an alleged loss of about 50 lakhs from the sale, calculating this loss at the difference between the face value of the shares allotted and the sale price of the Burma shares. The Income-tax authorities held that the transaction regarded as a purchase and sale of shares was illusory altogether, that the Appellant was not entitled to take the face value of its shares as the price paid for Burma shares and that as the market value of the Burma shares on the date of the agreement to purchase was only Rs. 98-14|17, there was really no loss but a profit. On a reference to the High Court under Sec. 66 of the Income-tax Act, the High Court upheld the assessment. On appeal to the Privy Council,

HELD, that the real value objectively of the shares of the Appellant Company would not be their nominal or face value but only the intrinsic value of the Burma shares exchanged therefor, as a company by the issue of a share credited with a definite sum as paid thereon would not become a debtor to its shareholder in respect of that full amount and that consequently no loss was sustained by the Appellant.

HELD, further that as the agreement did not embody in any real sense a purchase of the Burma shares but only a right to receive a sum of money being their sale proceeds, the Appellant did not sustain any loss, the English Companies remaining liable for the discount materialised by the sale, at which the Appellant Company's shares must be held to have been issued.

Moseley v. Koffyfontein Mines, Ltd, (1904), 2 Ch. 108, Applied.

Before a question is entertained by the High Court under Sec. 66 of the Income-tax Act, the preliminary statutory requirements thereunder must be strictly complied with.

Scope and limits of the applicability of the rule in In re. Wragg discussed.

Appeal [Privy Council Appeal No. 36 of 1929] preferred against the judgment of the High Court at Bombay (Martin, C. J., and Crump, J.), reported in 3 I. T. C. 105.

A. M. Salter and C. W. Turner, for the Appellants.

A. M. Dunne and R. P. Hills, for the Respondent.

JUDGMENT.

LORD BLANESBURGH:—This is an appeal from a judgment of the High Court of Judicature at Bombay, upon a reference made to that Court by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act, 1922. The substantial question for decision by the Board is whether the appellants are liable to pay Indian super-tax for the year 1924-25 on the footing that at the least they made no loss by, so that they are entitled to no credit in respect of, the realisation of a certain block of shares in the Burma Corporation (India), Limited, sold in January, 1924, in the circumstances now to be stated. The High Court have held them to be so liable. Hence this appeal.

The appellants, who will be referred to as the Indian Company, were incorporated under the Indian Companies' Act on the 10th February, 1920 with a nominal capital of seven crores of rupees, divided into 3,50,000 shares of 200 rupees each. Promoted as a private company by two English companies, the Share Guarantee Trust, Limited, and the Intercontinental Trust (1913), Limited, all the issued shares of the Indian Company, with the exception of one share taken by each of the two nominee subscribers to its Memorandum of Association, have throughout been held by one or other of the English Companies. Their joint control of the Indian Company has thus been in every respect and at all relevant times complete.

That Company was really established that it might acquire from the English Companies, as a single block of 312,817 shares, two separate holdings in the Burma Corporation, Limited, of 134,705 shares belonging to the Share Guarantee Trust, and of 178,112 shares belonging to the Intercontinental Trust. The nominal value of each of these Burma Corporation shares was £1. They were all fully paid, and they stood in the London market at the high price of £14 each.

The terms of their acquisition by the Indian Company were contained in two sets of agreements. To one set, one of the English Companies was party disposing; to the other set, the other. But the agreements of each set were of even date, and their terms were, *mutatis mutandis*, identical. Moreover, since their execution, the respective outstanding interests in the shares of the two disposing Companies have been dealt with as if theirs was the interest of a single person in the entire block. Accuracy, in the circumstances, will accordingly not be seriously endangered, while brevity and convenience of statement will alike be served if their Lordships in what follows proceed, unless otherwise stated, upon the assumption that the entire arrangement was embodied in a series of composite agreements made between the two English Companies on the one side and the Indian Company on the other.

It was by two such agreements executed on the 10th February, 1920—the day of its incorporation—that the Indian Company's interest in the shares originated.

The first of these two agreements resulted in a simple contract for the purchase by the Indian Company of the whole block of the Burma Corporation shares in consideration of the issue of an equal number of shares in the Indian Company credited as fully paid; and, as some form of reconstruction of the Burma Corporation was apparently then in prospect under which each share in the Corporation would in due course be exchanged for 14 shares in Burma Corporation (India), Limited, the agreement contained a provision that if this exchange took place, prior to completion, the sale and purchase should apply to the shares so exchanged. The effect so far was that the Indian Company acquired 312,817 of

Burma Corporation shares of £1 each, or their equivalent, in consideration of the issue of 312,817 of its own shares credited as fully paid. And the two separate agreements embodying that result were duly filed.

But the real transaction was contained in the second of the two composite agreements already referred to, the terms of which were not intended to be filed, and were not filed.

By this second agreement, subsequently referred to between the parties and here as the principal agreement, out of the 312,817 shares of the Indian Company representing the then consideration for the Burma shares, one-half—or 156,408 shares—were to or by direction of the respective English Companies to be allotted immediately, while the remaining shares were to be allotted at the rate of one share for each two shares of the Burma Corporation as delivered to the Indian Company. Somewhat inconsistently 25,000 shares in the Burma Corporation were to be delivered to the Indian Company forthwith, while delivery of the “undelivered shares”, as prescribed, was to be made on such dates as might be mutually agreed. The whole were, however, to be delivered within three years—that is before the 10th February, 1923. In the meantime possession of the undelivered shares was to be retained by the English Companies, and during the period prior to completion these companies were given power from time to time to deposit and charge the shares for their own liabilities joint or several or for their liabilities jointly with any other parties up to a limit of two and one-half million pounds sterling. The English Companies were also, by a clause numbered 4, given power with the consent of the Indian Company to sell any of the undelivered shares and either to utilize the proceeds of sale in discharge of such liabilities, in which event—and this, as will later appear, was a significant provision—the purchase consideration was to be “proportionately reduced”—or to remit the proceeds to the Indian Company, in which event “the equivalent purchase consideration for the shares”—another significant provision—was to be duly allotted.

The 156,408 shares of the Indian Company credited as fully paid were duly issued by that Company as provided by the principal agreement. It would not have been easy to harmonize with the other provisions as to allotment the immediate delivery to the Indian Company of the 25,000 Burma Corporation shares. But this difficulty was not allowed to arise for neither these shares nor, indeed, any Burma shares at all were ever delivered to the Indian Company. On the 10th February, 1923, the day of expiration of the period limited for completion, all that had happened was that three years before 156,408 shares of the Indian Company had been issued as fully paid, and, so far, for nothing.

With these circumstances unchanged a further composite agreement was, on the 14th November, 1923, come to by the parties, supplemental to and by way of variation of the original arrangement. By this time the 312,817 shares of the Burma Corporation, Limited, had become 4,379,438 shares of the Burma Corporation (India), Limited, of Rs. 10 each; and by the arrangement as now modified it was provided that these shares need not any of them be delivered before the 10th February, 1926; that the English Companies, with the general or special authority of the Indian Company might sell any of the shares and should in that event on completion pay to the Indian Company the proceeds of sale, together with all dividends received on the shares and clause 4 of the principal agreement above referred to was modified accordingly. In consideration for this, it was agreed by the English Companies—and this was a modification of the first importance—that the purchase consideration mentioned in the principal agreement should not in any case exceed the 156,408 shares already allotted as above stated.

In a case like the present where the Indian Company was throughout merely another name for the English Companies acting in concert, it would perhaps have been remarkable if these arrangements, elastic as are their terms, had not been worked out so as best to meet the convenience of the two English Companies. And so they plainly were. The shares sold remained in the respective names of the two companies, who between them received and retained all the dividends; when the shares were sold they received and retained the entire purchase price: it was only after their sale, actually effected in 1924, that these receipts were even brought into the accounts of the Indian Company; and even this seems to have been little more than a book entry, for, as appears from the evidence of Mr. Sandeman, a director of that Company, no part either of the purchase price or of the dividends had even then been received in India. They remained in England, presumably under the control of the English Companies, and as late as December, 1926, they were according to his statement, still there.

But this course of dealing, independent as it was of the Indian Company, really involved little more than a generous interpretation in the English Companies' own interests of the actual provisions of the agreements themselves which, properly understood, embodied an arrangement of a most unusual description in no way characteristic of the simple transaction of purchase and sale set forth in the filed agreements.

The agreements left the English Companies with, in effect, the same dominion over the shares as they enjoyed before their so-called sale. With the consent of the Indian Company, which was the merest formality, the English Companies might sell the shares; without even that form of consent, they might pledge them for their own debts or for the debts of themselves or other parties for a sum or sums up to as much as 2½ million pounds. Had the English Companies pledged the shares up to that limit, and had their value fallen below it—and their value did fall far below it by the beginning of 1924, if not before—it would have been open to the English Companies within the terms of their agreements to withdraw the shares from the Indian Company altogether and retain, for nothing, their 156,408 fully paid shares in that Company. Further, if they sold any of the shares, at whatever price, on tendering that price, however small, they were entitled to one fully paid share of the Indian Company for every 28 rupee shares sold, whatever the discount involved. Finally—and this was the event which happened—on a sale of the shares under the 1923 agreements and on their accounting for the proceeds, the English Companies were entitled to retain the whole of their 156,408 issued shares irrespective of the excess of their par value over the only sum received by the Indian Company in respect of them. As a matter of fact the deficiency below par value on the realisation in 1924 amounted to as much as Rs. 50,04,972, representing a discount of approximately Rs. 32 on each of the 156,408 shares of the Indian Company.

In truth the agreements did not in any real sense embody a purchase of the Burma Corporation shares by the Indian Company, in consideration of the issue of fully paid shares of that Company. More truly the so-called purchase was an elaborate arrangement under which while, it is true, the Indian Company might in certain events have received delivery of the Burma Corporation shares in specie, it was just as likely that the Indian Company, getting everything to which under the agreements it was entitled would receive a sum of money only, a sum which it was under the arrangement bound to accept in satisfaction whatever its amount might be. And, if their Lordships may here conveniently so far anticipate, the Indian Company has in the events received, and has duly received money only for its shares so issued as fully paid. And not only so,

but it has received a sum, less than the nominal value of the shares by the above figure of Rs. 50,04,972, or Rs. 32 each.

In the actual result, therefore, the shares have been issued by the Indian Company at a discount of that amount, and as this is the sum which in this litigation and upon this appeal the appellants, the Indian Company, contend represents the loss sustained by them in respect of this transaction, it is convenient to ask at once whether, even as so far stated by their Lordships, the facts do not furnish an immediate refutation of that contention.

It is, of course, necessarily grounded on the assumption that these issued shares of the Indian Company are in the hands of the English Companies fully paid and free from any liability for calls or otherwise. If the English Companies remain between them liable for the discount which has in fact now materialized then it necessarily follows—for no doubt as to the solvency of either English Company is suggested—that the Indian Company has sustained no loss at all. And upon the facts, as just detailed, that liability is, in their Lordships' judgment, fixed upon the English Companies by the application to this case of the principle enunciated by the Court of Appeal in the case of *Moseley v. Koffyfontein Mines, Limited*.⁽¹⁾, where it was held that if an arrangement for the issue of shares is such that in the course of its due working out there is as much as a possibility that in the result the shares will have been issued at a discount, then the issue of the shares as fully paid cannot be justified. Here such a discount has in the result actually materialised; its very amount has been ascertained, and their Lordships, applying as they do, the principle just stated, reach the conclusion that the Indian Company's alleged loss has not been proved, and that its present appeal on this simple ground must fail.

But while this view was foreshadowed by the learned Commissioner, neither in the High Court nor in the arguments before the Board was the case dealt with so simply. Their Lordships accordingly will proceed to consider its further aspects.

The English Companies never, it seems, exercised their power of pledging the Burma shares. They retained them all, until in January, 1924, they sold them in England at 8s. a share, or Rs. 6 according to the then rate of exchange—making a total consideration of Rs. 2,62,76,628. This is equivalent to a price of £5:12s. for each £ share in the original Burma Corporation. These shares were, as has been stated, worth in British currency £ 14 each in February, 1920, and there can be no doubt that the English Companies have, by entering into their agreements with the Indian Company, sustained in England a very serious loss which they would have been spared had they in February, 1920, disposed of their Burma shares upon the open market. Nor can their Lordships doubt that this loss has really provoked the complaint made by the Indian Company in this case. But although the English Companies are the Indian Company's only shareholders, the question here is not whether the English Companies have sustained a heavy loss, but whether the Indian Company has sustained any loss at all. And on the assumption which their Lordships now make that the Indian Company's shares must be treated as fully paid that question depends upon the price which on that footing the Indian Company must be taken to have paid for the Burma shares. Did it exceed the sum finally received for them? That is the issue.

Now it is common ground between the parties that the intrinsic value of the Indian Company's shares on the 10th February, 1920, on the footing that the

(1) (1904) 2 Ch. 108 at p. 118.

the Company was then entitled to a free Burma Corporation £1 share for each of its 312,817 shares issued or to be issued was, at the then high rate of exchange, Rs. 98 only. How far that value would stand to be reduced if each Burma share instead of being "Good delivery" was one subject to the reservations and so forth of the principal agreement has not been gone into, and it need not for the present purposes be here explored. Rs. 98 may without deduction be taken to be the value of each of the 156,408 shares issued in February, 1920, on the footing on which they were then issued. And in the first stages of their present dispute with the Revenue, the Indian Company, through its accountants, was prepared to adopt the then actual value of its shares issued as the criterion by which should be determined the question whether it had or had not sustained a loss on ultimate realisation. Its claim on this footing, however, was that the release on the 14th November, 1923, of the Indian Company's obligation to issue 312,817 shares or any shares beyond the first issue of 156,408, operated retrospectively to double the value in 1920 of these issued shares, so that each share must be taken to have then represented for the Company an expenditure of Rs. 196. When, however, it was pointed out that while this release of 1923 might enhance the then value of the issued shares in the hands of their holders, it in no way enhanced their value to the Indian Company in 1920, seeing that the shares had then been parted with once and for all, the alternative contention was put forward, on behalf of the Indian Company, and it was the contention placed before the Board, that the value to the Indian Company of its 156,408 shares at the date of issue must be taken to have been their nominal value of Rs. 200 each, no more and no less, on which basis the Indian Company has on realisation sustained, as is admitted, a loss of the above sum of Rs. 50,04,972.

The Indian Company's claim to have this loss allowed as a deduction from its super-tax assessment was in the first instance rejected by the Senior Taxing Officer, not however because the loss had not been sustained, but because in his view, it was a capital and not a revenue loss.

After a series of appeals, in the course of which the view was taken that in the circumstances no loss of any kind had been sustained, but, on the contrary, a large profit had been made by the Indian Company, the High Court finally, by order dated the 17th December, 1925, under section 66 (3) of the Act, directed the Commissioner of Income-tax to make a reference to the High Court of the following question of law arising out of the Indian Company's super-tax assessment for the year 1924:—"Whether the Commissioner of Income-tax was not bound in law to take as the price paid for the Burma Corporation shares the nominal value of the shares allotted (by the Indian Company) in payment therefor."

The Commissioner duly made the reference required and, on the matter coming before the High Court for hearing on the 5th October, 1926, that Court made an order purporting to be made in pursuance of section 66 (4) of the Act directing the Commissioner to deal in particular with a further question, namely, whether the alleged loss was a capital loss, and to find further facts and generally to amend the case. The Commissioner, after a further hearing of the parties, stated an additional case, and submitted to the Court two further questions, namely:—(A) Whether the alleged loss in question (if any) was a capital loss or revenue loss; and (B) Whether the alleged loss in question (if any) can be taken into account in view of the fact that it had accrued and arisen outside British India in view of the provisions of sections 4 (1) and (2) of the Income-tax Act, 1922.

Their Lordships propose now to deal only with the original question, although they must refer again to the circumstances in which the other two

were stated. With reference to that question, the Commissioner, in his original letter of reference, after stating that each share of the Burma Corporation had been admitted by the Indian Company's accountants to be worth only Rs. 98 on the 10th April, 1920, submitted that the only reasonable inference was that each share of the Indian Company was only worth that amount. This finding was not in question before the Board. In his second letter of reference dealing with the contention which had then been set up that the case of *In re Wragg*(1), required the nominal value of the shares issued and that alone to be taken, the Commissioner, after a full review of the arguments which their Lordships have already discussed, stated his conclusion of fact to be that the whole scheme was as a simple purchase and sale of shares, illusory.

The case then again came before the High Court, and on the 5th March, 1928, that Court pronounced the judgment from which the present appeal is brought. Its view broadly was that the Court was brought under no compulsion by the decision in *In re Wragg*(1), to take the nominal value of the shares allotted by the Indian Company as necessarily representing the price paid by that Company for the Burma shares. The present case, in the opinion of the learned Chief Justice, was within the exception to that decision stated by A. L. Smith, L.J., in his judgment in *In re Wragg*(1), for that here the parties had themselves in effect—so great was the discrepancy—acknowledged the consideration received to have no relation in point of amount to that nominal value. The real value of each share in the Indian Company as issued could not have exceeded Rs. 98. It might, if other dates were taken, be found to have been even less. It was open to the Court to ascertain the true value. On any computation thereof the case of the Indian Company failed. It had made no loss on realization: on the contrary it had made, expressed in rupees as was right, a large profit—a profit in respect of each of its 156,408 shares worth only Rs. 98 at their date of issue, of as much as Rs. 70.

Now their Lordships are in full agreement that the Indian Company's case failed, as the High Court thought. But if *Wragg's case*(1), has any application to the present, and if it could not otherwise be distinguished, their Lordships would not as at present advised be prepared to follow the High Court in so far as its final order was based upon the distinction there taken. As they understand the observations of Smith, L.J., referred to by the learned Chief Justice, these were confined to a case where upon the face of the agreement for the issue of fully paid shares it was made apparent that the actual consideration received by the Company was recognised as being definitely less than the paid-up capital issued in respect of it. The observations were not directed to a case like the present where that fact has to be ascertained, if at all, by extrinsic evidence.

But there appears to be a more certain ground upon which *In re Wragg*(1), if it has any application at all to the present question, may in the view of the Board be distinguished, and that is to be found in the conclusion of the learned Commissioner already stated, that the transaction here regarded as a purchase and sale of shares was illusory altogether. To a case of which so much can be said *In re Wragg*(1), has no application, and that conclusion of the learned Commissioner, as one of fact, was binding upon the High Court as it is also binding upon the Board, supported as it is by ample material, to some of which attention has already been called earlier in this judgment.

Their Lordships, however, do not wish it to be supposed that in their view the decision in *In re Wragg*(1), is in point here at all. Even if, on any application by the Indian Company to make the English Companies liable to contribute

(1) (1897) 1 Ch. 796.

in respect of the shares issued to them, these Companies could successfully rely upon *In re Wragg*(1) as a defence, that result in their Lordships' opinion would have no influence upon the fortunes of the appellants' present appeal.

In re Wragg(1), was one of many cases—*In re Almada and Tiritto Company*(2), *Ooregum Gold Mining Company v. Roper*(3), *The Eddystone Marine Insurance Company*(4), are other notable examples—in which the question, always as between a Company or its Liquidator on the one hand and the allottee of the shares issued as fully paid on the other, was whether in his hands the shares were held free from liability for calls or otherwise. There is no such question here. To this litigation, the English Companies, the allottees of the shares, are not parties, nor in law, are they even privies. The issue is one between the Revenue and the Indian Company only, and the sole question now is what was the real value objectively of the fully paid shares issued to the English Companies by the Indian Company at the date when they were in fact parted with. It is not disputed by the appellants the Indian Company, that the intrinsic value of these shares, if it had then exceeded their nominal value would have had to be returned as their true value. But their contention is that if, although judged by the same tests, their intrinsic value was then less than their nominal value, that last value, and no less, must be returned as their true value. This, they say, is the result of *In re Wragg*(1).

Their Lordships have some difficulty in grasping the argument. First of all, it is clear that there are some limitations to be placed upon the influence of *In re Wragg*(1). If, for example, the shares here had been issued to an individual who died on the next day, it could hardly even have been contended that by reason of *In re Wragg*(1), his estate would be charged with death duties in respect of any other than the real value of the shares whether that value was above or below their nominal value. Again, if immediately after the issue of the shares here the Company, upon proper resolutions passed, had presented a petition for the reduction of its capital on the ground that except to the extent of Rs. 98 per share its issued capital of 156,408 fully paid was unrepresented by available assets, can it be supposed that *In re Wragg*(1), would, of itself, have been any obstacle to an order confirming the reduction being made? Why then should that decision stand in the way of the real value of the shares being now in like manner ascertained? Their Lordships can only suppose the answer to be that the view is subconsciously assumed that a company by the issue of a share credited with a definite sum as paid thereon, becomes in some sense a debtor to its shareholder in respect of that full amount. But of course that is not so. A company is in no sense debtor to capital. *Lee v. Neuchatel Asphalte Company*(5), *Verner v. General Trust*(6). The amount credited upon a share may, as between one shareholder and another, while the Company is a going concern, determine the proportion of profits receivable by him as dividend, and, in a winding-up, his proportion of surplus assets. But it has no influence to extend or increase the aggregate amount available for division in due course of administration amongst the whole body of shareholders; nor does it make the company a debtor for any sum at all.

In their Lordships' judgment accordingly the decision in *In re Wragg*(1), ought to have no influence upon the question now raised, so that, however its claim be regarded, this appeal of the Indian Company fails.

Before parting with the case their Lordships think it right to allude again to the presentation to the High Court of the two additional questions to which they have already made reference, but which it is unnecessary for them further

(1) (1897) 1 Ch. 796.
(3) (1892) A. C. 125.
(5) 41 Ch. Div. 1.

(2) 38 Ch. Div. 415
(4) (1893) 3 Ch. 9.
(6) (1894) 2 Ch. 239.

to consider. In the present case the only result of the presentation of these two questions was that a final decision of the case, on the first and only essential question, was delayed for nearly a year and a half and much additional expense was incurred. Their Lordships are fully alive to the circumstances in which the High Court was constrained to direct that these further questions should be referred to it for consideration, and the result in the present case of the order then made merely serves to confirm the view of the Board that the High Court will, in future cases, be well advised to require, before they seek to entertain any questions under section 66 of the Indian Income-tax Act, that the preliminary requirements of the section are strictly complied with.

The stringency of these requirements is clearly deliberate. It is the intention of the enactment that the High Court is not to be flooded with such applications. The object is salutary and in their Lordships' judgment the High Court will be well advised, before they entertain any question under the section, always to see that the preliminary statutory conditions have been fully observed.

Upon the whole case, for the reasons they have given, their Lordships will humbly advise His Majesty that this appeal be dismissed with costs.

E. F. Turner & Sons, Solicitors for the Appellants.

The Solicitor, India Office, Solicitors for Respondent.

(360) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Justice Sir Leonard Adami, Kt., and Mr. Justice Kulwant Sahay.

[10th February, 1930]

Ganesh Das Kalu Ram

.. Assessee.

v.

The Commissioner of Income-tax, Behar and Orissa.

Indian Income-tax Act (XI of 1922), Sec. 66 (2) and (3)—Application for reference after one month—Copy application for Assistant Commissioner's order struck off—Application to High Court, maintainability of.

Where the assessee who allowed his copy application for the Assistant Commissioner's order to be struck off for non-prosecution applied to the Commissioner for reference under Sec. 66 (2) more than a month after the Assistant Commissioner's order and the Commissioner dismissed it as time barred,

HELD, that the application to the High Court under Sec. 66 (3) was not maintainable.

JUDGMENT.

This application must be dismissed on the preliminary objection on behalf of the Crown.

An application was dismissed by the Assistant Commissioner of Income-tax on the 19th February 1929 at Cuttack in the presence of the petitioner or his pleader. On the 18th March 1929, the petitioner applied for copy and received information what number of folios was necessary. No further steps were taken by the petitioner and so on the 3rd April the application for copy was struck off the file. On the 4th April the petitioner made an application under section 66,

sub-section (2). The Commissioner on the facts refused to admit the application on the ground that it was barred since section 66, sub-section (2) allows of only one month from the date of the passing of an order under section 31 or under section 32. This being so, under sub-section (3) of section 66 the petitioner could not come up to this Court for assistance.

It has been argued before us that time ought to have been allowed for obtaining a copy of the order of the Assistant Commissioner and it should have been excluded in reckoning limitation. But the learned Advocate for the petitioner is unable to state before us how he got a copy of the order or what time it took to get it. The record shows that he took no steps to get the required copy.

The application must be dismissed with costs: hearing fee two gold mohurs

(361) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

*Before Sir Guy Rutledge, Kt., Chief Justice, Mr. Justice Ormiston
and Mr. Justice Brown.*

[28th February, 1930]

K. K. C. T. Chettyar Firm

.. Assesseees.

v.

The Commissioner of Income-tax, Burma

.. Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 10 (2) (iii)—Partnership deed—Provision for taking loans from partners—Partners' investments, if genuine loans—Interest in respect of partners' loans, claim for deduction of.

Under a partnership deed in respect of a money lending business the partners were to contribute equally the capital amount of Rs. 27,500 and to invest in deposit as fixed or temporary loans for the business such sums of money at their command at such rates of interest as may be agreed upon, these loans to be distinct from the original capital and to be treated on the same footing as borrowings from strangers. On an assessment to income-tax the firm claimed deduction of the interest paid in the account year to the partners on their investments. This claim was disallowed on the ground that having regard to the smallness of the original capital, the absence of any document evidencing the loans and the large borrowing from Banks, the partners' investments were merely surplus capital and not genuine capital loans to the firm.

HELD, (1) that the Income-tax authorities were not entitled to hold that the investments in the firm in the names of the partners did not represent genuine borrowings by the firm,

(2) the sums credited to the partners in the firm's accounts as interest on capital borrowed from them was an admissible deduction under Sec. 10 (2) (iii) of the Income-tax Act.

CASE.

I have the honour to refer to the High Court under section 66 (2) of the Indian Income-tax Act, 1922, questions of law arising out of the order under section 31 on the appeal of the K. K. C. T. Chettyar Firm, Rangoon (hereafter called the firm), against its assessment for the year 1928-29.

2. The facts are as follows:—

(a) The firm which carries on a money-lending business at Rangoon consists of two partners both Hindu undivided families—K. K. C. T. Chidambaram Chettyar and his sons: A. R. S. A. Narayanan Chettyar and his brother.

(b) A copy of the deed of partnership, dated 9th July 1926 is attached and marked A*. According to this deed each partner has a half share in the partnership and each has contributed half of the total shop capital of the partnership which is Rs. 27,500. The deed further provides that each partner may lend money to the partnership, such loans to be treated on the same footing as loans taken from strangers. The provisions of this deed were in force at the time of the assessment.

(c) For the year 1928-29 the Income-tax Officer assessed the firm on an income of Rs. 80,302. A copy of his assessment order is attached and marked B.* The item in dispute out of which this reference arises is a sum of Rs. 26,017-0-3 made up of two sums of Rs. 8,369-1-9, and 17,647-14-6 shown in the firm's accounts as paid to the first and second partners respectively as interest on investments standing in their names in the books of the firm. This item was disallowed as being interest on the surplus capital of the partners not admissible under section 10 (2) (iii) of the Act. This disallowance was upheld by the Assistant Commissioner on appeal. A copy of the appellate order is attached and marked C.*

(d) The Income-tax Officer found that the money employed by the firm in its business consisted of Rs. 11,45,800 made up as follows:—

	Rs.
Shop capital	.. 27,500
Investments in the name of 1st partner	.. 86,000
Investments in the name of 2nd partner	.. 1,82,300
Loans from banks in Madras	.. 4,00,000
Loans from banks in Rangoon	.. 3,00,000
Other liabilities	.. 1,50,000
	<hr/>
	11,45,800
	<hr/>

3. For the firm it is contended that the following question of law arises out of the Assistant Commissioner's order and I am asked to refer it to the High Court:—"Where a partner in addition to the initial capital subscribed by him lends to the partnership a certain sum of money on the distinct understanding that in respect of this loan he is to receive interest from the partnership, whether such interest paid to the partner on such sum is a legitimate item of business expenditure within the meaning of section 10 (2) (iii) of the Income-tax Act, 1922, in the computation of income of the firm."

As I find myself unable to admit that we have in this case a genuine borrowing of money by the firm from its partners I cannot refer the question in this form. On the view I take of the facts two questions of law arise and I would refer them as follows:—(1) Whether the Commissioner of Income-tax is entitled to hold in this case that the investments in the firm in the names of the partners do not represent a genuine borrowing of capital by the firm? (2) If the Commissioner cannot so hold, is the sum of Rs. 26,017-0-3 credited to the

partners in the firm's accounts as interest on capital borrowed from the partners an admissible deduction under section 10 (2) (iii) of the Income-tax Act?

4. I have come to the conclusion that the investments in question are not genuine borrowings of capital by the firm. I am moved to the conclusion by various facts. The first is the very small amount of shop capital. It appears to me that this is a merely nominal sum having no relation whatever to the business which has been done by the firm for many years past. It is in the circumstances just as much a nominal sum as if the firm had entered a sum of Rs. 2 as its capital. And if it is not open to this Department to find that a sum so small as this sum of Rs. 27,500 is nominal when it represents only 1/40th of the amount of capital used in the business and only 1/10th of the total investments of the partners in the business, then it would be possible for any firm to contend successfully that the whole of its capital with the exception of a rupee or two is borrowed. The next consideration is that there is no document such as a pro-note evidencing the loan. Reliance is placed on the entries in the accounts and the stipulation in the deed of partnership regarding loans by partners but since the firm's contention is that these are loans on the same footing as loans from strangers I do not see why pro-notes were not executed as they would have been if the money was borrowed from strangers. Another point is that on such a small nominal capital the firm would not be able to raise seven lakhs from the banks unless they could show that the partners had much more than Rs. 27,500 invested in the business. The facts taken as a whole seem to me to show that this is not a genuine borrowing of capital. The only point in favour of the firm's contention is that in spite of the disproportion between the amounts of extra capital put in by the two partners, each of them still gets a half share in the profits. But the amount of profit realised from these investments after interest is paid on them is of no great consequence. The important thing is the interest.

5. If the High Court holds that there is no evidence on which I can find as a fact that this is not a genuine borrowing of money by the firm, I still submit that the item in question is disallowable since it does not fulfil the conditions prescribed in section 10 (2) (iii). That section allows interest on borrowed capital only where the payment of interest thereon is not in any way dependent on the earning of profits. In the case of a firm my submission is that the payment of interest to partners is dependent on the earning of profits in every case since if there are no profits, the only fund out of which the interest could come is the partner's own capital. In the case of a dissolution this would lead to the absurdity of a partner paying interest to himself out of his own capital. In the present case the shop capital is given as Rs. 27,500 and the interest claimed is almost as great. A loss in one year would wipe out the whole of the shop capital and then where is the interest on these investments to come from? If it is to be paid at all it must come from the partners' pockets and in that case the result would be that a partner would have to forego the amount of interest on his advances corresponding to his share in the firm—in this case a half.

6. The Madras High Court on a finding that there was a genuine borrowing of capital from the partners, decided that the interest on the amount borrowed is an admissible deduction under section 10 (2) (iii). But this decision appears to have overlooked the contrary decision in *In re Lalla Mal Hardeo Das*(1), and it is desirable that the matter should be decided by this Honourable Court for this Province.

Foucar, for the Assesseees.

Government Advocate, for the Crown.

JUDGMENT.

ORMISTON, J.:—This is a reference by the Commissioner of Income-tax under section 66 (2) of the Indian Income-tax Act, 1922. The K. K. C. T. Chettyar firm consists of two partners. The partnership deed, dated the 9th July, 1926, recites that the parties as partners have been carrying on business chiefly in money lending for about a decade in Mogul Street, Rangoon, under the style of K. K. C. T., “each party holding one half share in the partnership and contributing equal share of capital amounting to Rs. 27,500 in all.” Clause 3 sets out that the partners resolve, (a) that the partnership is to continue up to January, 1928 and thereafter as long as they desire to continue in partnership either in the same equal shares or otherwise, (b) to embark on business other than money lending as may from time to time be expressly agreed upon, and (c) “also each of us to invest as deposit on fixed or temporary loans such monies as we may command at such rates of interest between the partnership on the one hand and each of us on the other and such deposits or loans shall have nothing to do with the capital invested and be treated exactly on the same footing as any borrowing from strangers.” The natural construction of sub-clause (c) is that it should be read as if after the word “at such rates of interest between the partnership on the one hand and each of us on the other” the words “as may be agreed upon” had been inserted. An excellent reason for entering into a written partnership agreement would be that thereby the partners could secure the advantage of being a registered firm.

For the year 1928-29, (during which the provisions of this instrument were in force), the Income-tax Officer assessed the firm on an income of Rs. 80,302. An item of Rs. 26,017-0-3 made up of two sums of Rs. 8,369-1-9 and Rs. 17,647-14-6, is shown in the firm's accounts as paid to the first and second partners respectively as interest on investments standing in their names in its books. The firm claimed that this item should be treated as an allowance under section 10 (2) (iii) of the Act as being the amount of interest paid “in respect of capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits.” The Income-tax Officer held that the item was interest on the “surplus capital of the partners” and was not admissible as an allowance under section 10 (2) (iii). The firm appealed to the Assistant Commissioner who, acting under section 31, confirmed the assessment. The firm applied to the Commissioner under section 66 (2) for a reference to the Court of a question of law arising out of the order. The Commissioner refused to refer the question in the form asked for by the firm. He referred two questions: (1) Whether the Commissioner of Income-tax is entitled to hold in this case that the investments in the firm in the name of the partners do not represent a genuine borrowing of capital by the firm? (2) If the Commissioner cannot so hold, is the sum of Rs. 26,017-0-3 credited to the partners in the firm's accounts as interest on capital borrowed from the partners an admissible deduction under section 10 (2) (iii) of the Indian Income-tax Act?

The Income-tax Officer found that the money employed by the firm in its business was Rs. 11,45,800 made up as follows:—

	Rs.
Shop capital	27,500
Investments in the name of 1st partner	.. 86,000
Investments in the name of 2nd partner	.. 1,82,000
Loans from banks in Madras	.. 4,00,000
Loans from banks in Rangoon	.. 3,00,000
Other liabilities	.. 1,50,000
	<hr/>
	11,45,800

The Commissioner has come to the conclusion that the investments in question are not genuine borrowings of capital by the firm, and this for 3 reasons. In the first place he points to the very small amount of shop capital and is of the opinion that it is a merely nominal sum having no relation whatever to the business done by the firm. He argues that, if it is not open to the Income-tax Department to find that this sum of Rs. 27,500 which represents only 1/40 of the capital used in the business, is a nominal sum, it would be possible for any firm to contend that the whole of its capital with the exception of a rupee or two is borrowed. He next observes that there is no document such as a promissory note, evidencing the loan and says that, it being the firm's contention that the loans by the partners were on the same footing as loans by strangers, he does not see why promissory notes were not executed as they would have been if the money had been borrowed from strangers. His third reason is that on such a small nominal capital the firm would not be able to raise Rs. 7,00,000 from the banks, unless it could show that the partners had much more than Rs. 27,500 invested in the firm.

Assuming that the investments are genuine borrowings, the Commissioner is of the opinion that the item in question is disallowable since it does not fulfil the conditions prescribed in section 10 (2) (iii). His view is that in the case of a firm, the payment of interest to partners is dependent on the earning of profits in every case, since, if there are no profits the only fund out of which the interest can come is the partner's own capital. In the case of a dissolution, he says, this would lead to the absurdity of a partner paying interest to himself out of his own capital. In the present case the interest claimed is almost as great as the shop capital. A loss in one year would wipe out the whole of the shop capital. If the interest on the investments is to be paid at all, it must, he says, come from the partners' pockets and in that case the result would be that a partner would have to forego the amount of interest on his advances corresponding to his share in the firm—in this case a half.

The Commissioner has made the present reference in view of an assumed conflict between decisions of the Allahabad and Madras High Courts.

Mr. Foucar put forward an argument, based on section 66 (2) of the Act, that in a reference to the Court under that sub-section, it is not open to the Commissioner to come to any finding of fact, and that the only facts which the Court is entitled to consider are those found by the Assistant Commissioner who decided the appeal under section 31. In my opinion, it is not necessary to do more than refer to this contention, for in the present instance the case as stated by the Commissioner affords ample materials for answering the questions referred by him.

That a partner may make advances to his firm independent of his share in the capital thereof is clear law and is not in dispute. See Lindley on Partnership, (9th Edition), pages 407, 478.

In *In re Lalla Mal Hardeo Das*(1), a firm claimed that interest paid on account of money advanced by the partners for the purposes of the business should be reckoned as an allowance under section 10 (2) (iii). The partnership deed, (clause 13), provides that "whatever capital be needed for the joint business of the firm it will be paid in by the shareholders according to their shares." The Assistant Commissioner who examined the books of the firm reported that the money in respect of which the interest was charged in the account was not really "capital borrowed for the purposes of the business, but represented only

(1) 1 I. T. C. 266.

an advance of capital by the partners." The question referred was "Is the sum paid as interest to a partner for capital put into a firm an allowance admissible under section 10 (2) (iii)?" The answer was "No, such interest represents merely an assignment of a part of the net profits for the year in favour of partners who are regarded as entitled to such assignment by reason of special advances of capital made by them in the course of the year." The learned Judges went on to observe that the question whether there has been an advance of capital by particular partners or a *bona fide* borrowing of money by the firm in which the lender happens to be a partner must be treated as one of fact in every case.

This case is of little assistance, for clause 13 of the partnership deed amply supported the Commissioner's finding that the money in respect of which the interest was paid was not capital borrowed but represented only an advance of capital.

Subramaniam Chettiar v. Commissioner of Income-tax, Madras(1), is directly in point. The headnote is as follows: "Where a partner as partner genuinely lends money, beyond the initial capital, to the partnership at an agreed reasonable rate of interest and the money is used for capital expenditure, the interest paid by the partnership to him in the year of assessment must be deducted in computing the profits or gains of the partnership as provided by section 10 (2) (iii) of the Indian Income-tax Act." The facts are similar to those in the present reference. There was a partnership deed between two Chettyars according to the terms of which three-fourths of the agreed initial capital of Rs. 21,000 was contributed by the senior partner and one-fourth by the junior partner. They were to share the profit and loss in the same proportions. The document also contemplated that, if necessary, further sums might be contributed by either party towards the additional capital of the business and that interest should be charged upon it. The Commissioners found that the senior partner advanced a sum of Rs. 4,01,251 as additional capital in parts at various times and that the junior contributed comparatively a very small sum. The amount of interest on the senior partner's advances was Rs. 40,757, and that on those of the junior partner Rs. 78. The firm claimed deduction of these two items under section 10 (2) (iii). The Assistant Commissioner held that the whole of the additional sums advanced by the partners must be regarded really as the capital of the firm. On appeal the Commissioner in his order conceded that a partner may sometimes occupy a dual capacity, that is, he may lend a definite sum of money on a formal document, in which case it would be regarded as a loan, but he was of the opinion that in the case before him the sums advanced by the partners must be regarded, not as loans, but as "surplus capital."

The Vakil for the Commissioner argued that, though a partner may make a loan to the partnership, he cannot lend capital to it and that additional capital required for the purpose of the partnership can be borrowed only from outsiders; in other words, that though capital can be borrowed from outsiders, it cannot be borrowed from a partner. Dealing with this argument, Coutts Trotter, C. J., and Ramesam, J., who delivered the leading judgment, observed that the sub-clause itself did not contain any limitation as to the person from whom capital was to be borrowed and that once it is conceded that a partner can lend money just like any other third person, it is difficult to see why he cannot lend capital also. They went on to say:—"The Commissioner seems to think that if a sum of money is deposited with the partnership tem-

porarily for reasons unconnected with the business, it is a loan, but if it is invested for a much longer time than the business required it, the initial capital being insufficient then it becomes surplus capital and not a loan. All sums lent to the partnership are loans, whoever the parties are and whatever the purpose for which they are lent. After being borrowed if they are used like capital they become borrowed capital." In the case before them they held that the Commissioner himself having found that the sums were capital, there being no doubt that it was borrowed from the partners, section 10 (2) (iii) applied. The learned Judges then remarked on certain findings of fact by the Commissioner. The first was that the sums in question were not capital within the meaning of the sub-clause. This finding, they said, was based on facts which were common ground *plus* certain supposed legal principles for which there was no authority. "Whenever a sum is borrowed and it is afterwards used for capital expenditure, it is not open to the Commissioner to find that it is not borrowed capital as there is no such principle of law as is contended before us on behalf of the Commissioner." They made similar observations about the finding that from the beginning the initial capital was nominal and that from the beginning additional capital was intended. As to this they said that under the deed a partner was not bound to advance any additional capital, but that if he did so he was to get interest. It was not, therefore, open to ignore the difference between the characteristics of initial capital and of so-called surplus capital. The fact that a large business was contemplated for which the small initial capital would not be enough and additional capital would therefore be required had no bearing on the legal aspect of the question, additional capital having different incidents from initial capital. A further reason why it was not open to regard additional capital as really initial capital was that a difference between the amounts contributed by the partners would have no bearing on the proportion in which the profits are taken. "The Commissioner's findings being based on misconceptions of law cannot be accepted as findings of fact binding upon us." On the question whether interest paid on the advances can be said to be "in any way dependent on the earning of profits" they said that section 10 (2) (iii) applies if interest is payable whether profits are earned or not.

Wallace, J. agreed with this judgment, the case being one where on the facts found there was a genuine borrowing of capital at the prevailing market rate of interest. He made the reservation that in other cases it might not fall to be decided as a point of fact whether the alleged borrowing of capital was not a genuine loan but a mere device to evade the Act. He instanced the extreme case of a partnership with a nominal capital when the partners lend additional capital at a fancy rate of interest obviously designed to absorb all probable profits and thus enable them to submit a nil profits return. Beasley, J. also agreed and made the same reservation.

Tiruvengkata Achariyar, J. in a concurring judgment said that it is a question of fact in each case whether the further advance made by a partner over and above the capital agreed to be put in by him is really a loan or an increase of his capital in the business made with the consent of the other partners. In the case under reference, he observed, the question referred treated the advances as loans made by the partner to the firm for being utilised as capital and there seemed to be no ground for questioning that fact.

On the first question referred Mr. Eggar contends that the test to be applied is that suggested by Wallace, J. whether the alleged borrowing is a genuine loan or a mere device to evade the Act. He says that in the partnership

agreement in the case under reference the rate of interest to be paid on advances is left to the discretion of the partners and that it is open to them from time to time to vary the rate after the advance has been made. The natural construction of the agreement is that, inasmuch as borrowing from partners is to be on the same footing as borrowing from outsiders, the rate of interest is to be fixed at the time the loan is taken and should not vary from that agreed upon during its currency. There is no suggestion in the reference to show that exorbitant interest has been charged, or that the rate of interest originally agreed has been varied during the currency of the loans. The reference rather assumes the contrary.

I myself, however, am of the opinion that the more correct view is that of Coutts Trotter, C. J. and Ramesam, J. with the qualification, implied in their judgment and expressed in that of Tiruvenkata Achariyar, J. that the question is whether a further advance by a partner is intended to be a loan or as an increase of his capital in the business. There is nothing to prevent a genuine business being carried with a nominal capital, the vast bulk of the capital being advanced by outsiders. If it be conceded that a partner may lend capital to the firm, what difference in law does it make that the vast bulk of the capital is advanced by the partners themselves? Mr. Eggar has cited a number of authorities to show that a partner cannot recover a debt due to himself from the firm without suing for an account. For the purposes of this reference it is unnecessary to express an opinion on the point. If there is a liability by the firm to a partner the manner in which it is to be enforced is immaterial. If in any year there is a loss the partners individually are under an obligation to put the firm in funds to pay the creditors and amongst the creditors are the individual partners who have made advances.

I now turn to the so-called finding of fact by the Commissioner. To it the observations of the Madras High Court in relation to the findings of the Commissioner in the case before it are applicable. I have already dealt with the Commissioner's finding so far as it is based on the extreme case cited by him. I would only add that it is legitimate for partners to arrange the terms on which they will carry on business as they think proper. If it is thought inexpedient that they should have such liberty the matter is one for interference by the Legislature. The fact of the liability of a firm to its members is a fact entirely dependent on the mode of proof of such liability or whether it is secured and, if so, in what manner. The Commissioner's finding that the banks would not lend Rs. 7,00,000 to a firm which had only a capital of Rs. 27,500 is a mere speculation. A more probable speculation is that banks look to the credit of the individual partners rather than to the capital of the firm.

On the second question referred my view is that the payment of interest is in no way dependent on the earning of profits. I am unable to follow the reasoning of the Commissioner. It by no means follows that if there are no profits the only sum out of which the interest can come is the partner's own capital. For whether he has capital or not he is liable to put partnership in sufficient funds to pay the interest. If he has no capital left he must find the money from other sources. A simple illustration will make the position clear. Supposing that A and B are partners in equal shares. A lends the partnership Rs. 1,00,000, the interest on which is Rs. 10,000, and B lends it Rs. 50,000, the interest on which is Rs. 5,000. If there is a loss, the partners between them have to pay the partnership Rs. 15,000. Each partner pays Rs. 7,500. A receives back Rs. 10,000 and B receives back Rs. 5,000. This shows that the interest does not depend on the profits.

My answer to the questions referred is as follows:—(1) The Commissioner of Income-tax is not entitled to hold in this case that the investments in the firm in the names of the partners do not represent a genuine borrowing of the firm. (2) The sum of Rs. 26,017-0-3 credited to the partners in the firm's account as interest on capital borrowed from the partners is an admissible deduction under section 10 (2) (iii) of the Income-tax Act.

I would order the Commissioner to pay to the K. K. C. T. Chettyar Firm the costs of the reference, advocate's fee 10 gold mohurs.

RUTLEDGE, C. J.:—I agree.

BROWN, J.:—I agree.

There may be cases in which advances are made in the form of loans in such a manner and under such circumstances as to show that it was not the intention to treat these advances as loans, and in which it could be held that the advances were not really loans at all. But in the facts of the present case as stated there are no indications which would justify such a finding. There is no allegation here that the loans were not made at fixed rates of interest, or that there is anything abnormal in the manner in which the interest is paid. The advances must therefore be treated as loans, and the provisions of section 10 (2) (iii) of the Act must be held to apply.

(362) IN THE COURT OF THE JUDICIAL COMMISSIONER
AT NAGPUR.

Before Sir Charles Findlay, Kt., Judicial Commissioner.

(4th March, 1930).

Moulana M. E. R. Malak

.. Assessee

v.

The Commissioner of Income-tax, Central
Provinces and Berar

Indian Income-tax Act (XI of 1922) Secs. 10 (2) and 66 (3)—Atba-e-Malak Badar Community—Sums paid to community members employed in shops—Affidavits from members—Claim of disallowance—Reference to High Court.

The assessee, the Atba-e-Malak Badar Community, whose claim for deduction of sums paid to members of the community employed in their shops was disallowed by the High Court, subsequently filed affidavits signed by the alleged servants disclaiming any interest in the shops and claimed the same disallowance in the assessment for a subsequent year. On the Income-tax authorities ignoring the affidavits and negating the claim the assessee applied to the Court for a reference under section 66 (3) of the Income-tax Act.

HELD, that the filing of the affidavits immediately after the Court's adverse decision was an attempt to get round the Court's decision and there was no question of law requiring a reference to the Court.

Application [Miscellaneous Judicial Case No. 75 of 1929] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Central Provinces and Berar, to state a case for the opinion of the Court.

JUDGMENT.

This is an application under section 66 (3) of the Indian Income-tax Act requesting this Court to require the Commissioner of Income-tax to state the case and to refer it to this Court. The order of the Income-tax Commissioner in question is dated the 13th of August 1929, and this order, in turn, arose out of his proceedings for the assessment of the Atba-e-Malak Badar community to income-tax for the year 1928-29.

2. The question the Income-tax Commissioner was asked and refused to refer was couched in the following terms:—"Whether in view of the affidavits made by the members of the staff employed in Mehdi Bagh shops disclaiming any interest in the said shops, the Assistant Commissioner of Income-tax was justified in law in disallowing deductions of their salaries from the income assessed to income-tax." An appeal to the Assistant Commissioner of Income-tax was filed on the 21st of March 1929 and, in that appeal, the question of the disallowance of the amount disbursed for salaries was agitated. On the 23rd of May 1929 an affidavit signed by 11 alleged servants of the Community was filed; on the two following days further affidavits were filed. These were to the effect that the signatories were merely hired servants of Maulana Malak Sahib of Mehdi Bagh and that they had no right or interest in the property. The Assistant Commissioner, in his order, dated the 25th of June 1929, did not refer to these affidavits because, in his opinion, the point as regards salaries had already been agitated in this Court and decided on 18-4-29. The Assistant Commissioner of Income-tax accordingly did not refer at all to the affidavits in his order in question. As, however, the Commissioner of Income-tax points out the filing of the affidavits, in reality, amounted to an attempt to introduce new evidence before the Assistant Commissioner at a time when limitation had expired for the filing even of objections. The Commissioner of Income-tax very properly points out that it was only when the applicant had lost his case on the point involved in this Court that the affidavits in question were introduced, presumably as a kind of counter-blast, in the hope that they might benefit his case as regards the assessment for the year 1928-29.

3. The extraordinary procedure of the applicant (assessee) in the matter is only too obvious and I am wholly unable to see that there is, in reality, any question of law which can be referred to this Court for an answer in this connection. It is little less than extraordinary to note that the decision of this Court in Miscellaneous Judicial Case No. 25 of 1928 was passed on the 18th of April 1929* and then it was only thereafter that these affidavits were filed. In view of the decision of this Court, their evidential value obviously could amount to nothing and I am of opinion that the Assistant Commissioner of Income-tax was perfectly justified in rejecting them or ignoring them, which was, in effect, what he did. It is quite rightly pointed out that the matter in issue had already been decided by this Court and, if the assessee feels aggrieved by that decision, his remedy is by way of an appeal to their Lordships of the Privy Council.

4. I am, therefore, of opinion that the affidavits were utterly ineffective and deserve to be ignored and that, in view of the decision of this Court, the Income-tax authorities were correct in refusing to take any action on them. The

* Reported as 8 I. T. C. 468.

plea that a different year's assessment is now involved, is obviously a futile one because it is not urged that the constitution of the Community has, in the meantime, changed. I am unable, therefore, to see that there is any question of law whatever involved which could be referred to this Court. The affidavits in question, on the contrary, only suggest a somewhat stupid attempt to get round or render nugatory the decision of this Court already given on the question involved.

5. There is no ground, therefore, for the present application and it is dismissed. The applicant must bear the costs of the Income-tax Commissioner. I fix these at Rs. 100.

(363) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Agha Haidar.

(26th March, 1930).

Messrs. Deokinanden & Sons.

.. *Assesseees.*

v.

The Commissioner of Income-tax, Delhi.

..

Indian Income-tax Act (XI of 1922), Sec. 66 (3)—Joint family business—Separate business carried on by one member in partnership with strangers—Decision as to the business being family business—If res judicata—Reference to High Court.

The assesseees, a Hindu joint family firm, consisting of a father and son, on an assessment to income-tax claimed that a business carried on in the son's name in partnership with strangers was not a family business and that the decision in prior assessment proceedings that the son's share in the profits of this partnership was to be excluded in the computation of the assesseees' income was res judicata. On a consideration of facts of the case the Income-tax Officer disallowed the claim and added the partnership share income to the assesseees' other income for rate purposes. On an application to the High Court for a reference,

HELD, that the prior order apparently passed without investigation and enquiry would not debar the Income-tax Officer from re-opening that decision in the light of facts now come to light and that that order not having been set aside on capricious or frivolous ground, there was no question of law for a reference, to Court.

Sankaralinga Nadar v. The Commissioner of Income-tax, Madras, 4. I.T. C. 226; Followed.

Application [Civil Miscellaneous No. 608 of 1927], under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Delhi, to state a case for the opinion of the Court.

Kishan Dayal, for the Assesseees.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

TEK CHAND, J.:—This is a petition under section 66 (3) of the Indian Income-tax Act by the firm of Messrs. Deokinandan and Sons of Delhi asking this Court to require the Commissioner of Income-tax to state the case in respect of certain questions of law which it is alleged, arise on orders passed by the Income-tax authorities relating to the assessment of the petitioner for the year 1926-27 on the income of the "previous year."

The petitioner firm is owned by Chuni Lal and his only son Hanuman Parshad. The Income-tax Officer assessed the income of the petitioner firm at Rs. 32,485 to which he added, for rate purposes, Rs. 8,740 being the $\frac{3}{8}$ ths share of the profits derived by Hanuman Parshad from another firm Ghanisham Das Hanuman Parshad in which he was a partner and which had been separately assessed. The petitioner claimed a deduction of Rs. 5,928 as a bad debt against one Khushi Ram Munim and also urged that the profit earned by Hanuman Parshad as a partner of Messrs. Ghanisham Das—Hanuman Parshad should not have been taken to be the income of the assessee firm for rate purposes. The Income-tax Officer decided against the assessee on both these points and his order was confirmed on appeal by the Assistant Commissioner. The Commissioner refused to review the assessment or to make a reference to this Court under section 66.

After hearing Counsel at length I am of opinion that, on the facts as found in this case, no question of law arises. On the first point the contention on behalf of the assessee is that he was not given proper opportunity to place before the Income-tax Officer the necessary materials to show that the debt due from Khushi Ram was really a bad debt and had been written off during the accounting period. It appears, however, that a notice under section 23 (2) was duly issued to the assessee to produce or cause to be produced the evidence on which he relied in support of the deductions which he claimed. The petitioner failed to produce the necessary books which would have thrown light on the matter. In these circumstances he cannot complain that he was not given proper opportunity to prove his case. In this view of the fact it is not necessary to examine the question raised by Mr. Kishan Dayal, on the authority of a Full Bench decision of the Judicial Commissioners of Nagpur reported as *S. M. Chitnavis v. Commissioner of Income-tax, Central Provinces and Berar* (1) that the assessee's right to debit the loss sustained on account of bad debts written off by him, against the profits or gains of any year, is unqualified and absolute as regards the amount to be debited and the choice of time at which to write it off. This view is undoubtedly in conflict with the opinion of the majority of a Bench of this Court in *R. S. Puran Mal vs. Commissioner of Income-tax* (2), but the examination of this matter must be reserved for some other occasion, as the question does not arise on the facts of this case.

On the second question it is urged that there is no presumption under Hindu law that a business carried on by a co-parcenaar in partnership with strangers is a family business (*Mirza Mal Bhagwan Das v. Rameshar* (3)) and that the Income-tax authorities have misdirected themselves as to the law on this point. It is no doubt true that some of the observations of the Income-tax Officer and the Assistant Commissioner lend support to the suggestion that they did not raise the initial presumption in favour of the assessee, but there is no doubt that the facts mentioned by them (which are not denied by the petitioner's learned counsel before us) amply rebut that presumption. It is admitted that the firm Ghanisham Das Hanuman Parshad was started at a time when Hanuman Parshad

(1) 8 I. T. C. 321.

(2) 2 I. T. C. 286.

(3) I. L. R. 51 All. 827.

was an infant. It is also admitted that he is yet a student and is not doing any business separate and distinct from that of his father. There is no suggestion that he owns any property other than that of the joint family of which Chuni Lal and he are the only members, or that his share in the capital of the partnership came from a source other than the joint family funds. On these facts there can be no doubt that the initial presumption has been rebutted and the Income-tax authorities came to a correct conclusion in adding, for rate purposes, Hanuman Parshad's share of the profits in the firm Ghanisham Das Hanuman Parshad to the other income of the petitioner firm.

Lastly, it was urged, that in making the assessment for 1925-26 the former Assistant Commissioner, Mr. Lincoln had excluded Hanuman Parshad's share in the profits of this partnership from the income of the petitioner firm and that that decision debarred the Income-tax authorities from re-opening the same question again. In support of this contention reliance is placed on a recent Full Bench decision of the Madras High Court in *T. M. M. Sankaralinga Nadar vs. Commissioner of Income-tax, Madras*(1). In my opinion that decision does not help the petitioner. It was held there that when in a previous year of assessment a decision was arrived at after investigation and enquiry, that certain deductions ought to be made it is still open to the Income-tax authorities to re-open the question in a subsequent year of assessment, and the authorities not constituting a Court, are not barred by the principle of *res judicata*. It was also held that though they are entitled to re-open the enquiry they cannot arbitrarily change the assessment simply on the ground that the succeeding Officer does not agree with the preceding Officer's finding. "The principles of natural justice or judicial dealing which Courts impose upon Income-tax Officers would prevent them from capriciously setting aside the order of their predecessors based on an enquiry. But if fresh facts come to light which on an investigation would entitle the Income-tax Officer to come to a different conclusion from that of his predecessors he is entitled to re-open the question."

In my opinion, the law on the subject has been correctly laid down in this ruling and I venture to express my complete and whole-hearted concurrence with it.

In the present case, however, the order of Mr. Lincoln is a very brief one and was passed apparently without any investigation and enquiry. He did not notice the facts which have now come to light and which are mentioned in detail in the orders of the Income-tax Officer and the Assistant Commissioner. It cannot, therefore, be said that in disallowing the deduction, the Income-tax authorities have departed from any principles of natural justice or judicial dealing. Nor can it be urged that the order of Mr. Lincoln has been set aside capriciously or on purely fanciful grounds.

After a careful consideration of the whole case, I am of opinion, that no question of law arises in this case on which the Commissioner of Income-tax may be called upon to state the case under section 66 (3). I would therefore dismiss the petition. But having regard to all the circumstances I would leave the parties to bear their own costs of these proceedings.

AGA HAIDAR, J.:—I agree.

(363) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Agha Haidar.

(27th March, 1930).

Messrs. Bhola Shah Narsingh Das

.. Assessee.*

v.

The Commissioner of Income-tax, Punjab and

N. W. Frontier Provinces

.. Referring Officer.

Indian Income-tax Act (XI of 1922) Sec. 10 (2) (iii)—Loan by partner to firm—Interest thereon, if deductible in computation of firm's profits.

Where a partner of a firm as partner lends money to the firm beyond the initial capital at an agreed rate of interest and the money loaned is used for capital expenditure, the interest paid thereon by the firm to the partner is deductible under Sec. 10 (2) (iii) of the Income-tax Act in the computation of the profits and gains of the firm.

Subramaniam Chettiar vs. The Commissioner of Income-tax, Madras, 3 I. T. C. 187; Approved. In the matter of Lalla Mal Hardeo Das, 1 I. T. C. 272; Distinguished.

Case [Civil Reference No. 28 of 1929] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), by the Commissioner of Income-tax, Punjab and N. W. Frontier Provinces in compliance with the order of the High Court.

CASE.

In pursuance of the order quoted above I have the honour to refer the following case for the opinion of the High Court under section 66 (3) of the Indian Income-tax Act, 1922.

2. Facts of the Case.—The assessee is a firm of artists or commission agents constituted with the following partners:—1. Bhola Shah Labh Chand Four annas. 2. Narsingh Das Buta Mal Four annas. 3. Jagan Nath Four annas. 4. Gian Chand Four annas. This firm is an unregistered firm for the purposes of the Income-tax Act. The first and second partners are also separately assessed to income-tax. The third and fourth partners are individuals whose income has not hitherto been found to be taxable. Clause 2 of the deed of partnership under which the assessee firm is constituted runs as follows:—"Rs. 5,000 have been invested as capital, to start with, in equal shares by Bhola Shah and Narsingh Das, on which no interest shall be charged. Any sums required further for the partnership business shall be supplied by Bhola Shah and Narsingh Das, so that there should be no loss in the business, and on such amounts as they advance over and above the said Rs. 5,000 they shall be entitled to interest at 7½ annas per cent." Clause 3 provides that ".....If Jagan Nath and Gian Chand put any money in the joint business, they will also get interest at 7½ annas per cent. per mensem." Clause 12 says that "in the event of the dissolution of the partnership each partner will be entitled to an equal share of the entire stock in the shop and the *ugrahi* (sundry debts) after recouping the entire amounts of capital."

For the year 1927-28 the Income-tax Officer, Gujranwala, determined the assessable income of this firm to be Rs. 5,281. In the course of the assessment the

* A. I. R. (1930) Lah 788 (2)

assessee claimed that the following amounts of interest paid to the partners of the firm should be deducted in computing the profits:—Bhola Shah Labh Chand Rs. 920-12-0, Narsingh Das Buta Mal Rs. 1,613-9-9, Jagan Nath Rs. 279-3-6 and Gian Chand Rs. 948-14-0. It may be observed that at the stipulated rate ($7\frac{1}{2}$ annas per cent. per mensem) the total amount of interest claimed, viz., Rs. 3,762, represents an investment of capital of approximately Rs. 67,000. The firm claimed that the initial capital consisted of Rs. 5,000 of which half was subscribed by the first partner and half by the second and that in accordance with the partnership deed any sums invested by these partners over and above the initial capital were ordinary loans bearing interest, and that any capital invested by partners 3 and 4 was also in the nature of loans to the firm. The Income-tax Officer disallowed the claim on the ground that the amounts on which interest had been paid did not represent loans to the firm but further investments of capital by the partners. The assessee appealed against the assessment to the Assistant Commissioner who upheld the decision of the Income-tax Officer in this respect. The Assistant Commissioner did, however, reduce the assessable income on other grounds to Rs. 4,824. Against the decision of the Assistant Commissioner the assessee filed an application to the Commissioner under section 66 asking that the following points of law should be referred for the opinion of the High Court: (a) Whether or not according to the true construction of the partnership deed Rs. 5,000 is the capital of the firm and any sums advanced by any of the partners over and above this amount are ordinary debts bearing interest; and (b) That the interest due or paid to the partners for such debts is not an income of the firm and could not be assessed as the income of the firm.

The Commissioner took up the case in the exercise of his powers of revision under section 33 and reduced the assessable income by a further sum of Rs. 211 but refused to interfere in regard to the interest on the capital of the partners; he ascertained however that the interest paid to the partners Nos. 1 and 2 had been also taxed in their hands by another Income-tax Officer and he therefore called for the records and modified those assessments by excluding the amounts in question from their taxable income. The assessee was not content with the Commissioner's decision and declined to withdraw his application under section 66 (2). The Commissioner thereupon took the application and recorded an order in which he held, following the ruling of the Allahabad High Court in the case of *Lalla Mal Hardeo Das Spinning Mills*, (1) that the question whether there has been an advance of capital by particular partners or a *bona fide* borrowing of money by the firm in which the lender happens to be a partner in the firm is a question of fact to be decided in the circumstances of each case. He, therefore, declined to refer the matter to the High Court. The assessee thereupon under section 66 (3) moved the High Court, who ordered a case to be stated.

3. *Question to be referred.* The question of law which I have been asked to refer has been formulated by the Hon'ble Judges, and is as follows:—“Where a partner as partner lends money beyond the initial capital to the partnership at an agreed rate of interest and the money is used for capital expenditure, should the interest paid by the partnership to him in the year of assessment be deducted in computing the profits or gains of the partnership within the meaning of section 10 (2) (iii) of the Income-tax Act”.

I would respectfully submit that the words “in the year of assessment” involve a slight inaccuracy. The interest was paid in the ‘previous year’, i.e., during the accounting period of which the profits are computed and are, in

accordance with section 3 of the Act, to be charged to tax in the year of assessment, which is usually the following year.

4. *Opinion of the Commissioner.* It is perhaps desirable to note in the first instance that this question only arises in the assessment of unregistered firms. The practical effect of the provisions for the assessment of a registered firm is that each partner's share of the profits is taxed in his hands, so that it is immaterial whether his share is regarded as consisting entirely of profits or partly of profits and partly of interest. An unregistered firm, on the other hand, is assessed in the same way as an individual, i.e. on a graduated scale depending on the income of the firm. The partners are not taxed on their shares in the profits, but those shares are merely taken into account in computing the 'total income' of each partner in order to determine the rate of tax to which he is liable. Thus, in the present case, the unregistered firm has been taxed on its income of Rs. 4,613 at the rate appropriate to that income, namely 5 pies in the rupee. If the deductions claimed were allowed, the income of the firm would be reduced to Rs. 851, which is below the taxable limit of Rs. 2,000. The sums paid as interest to partners Nos. 3 and 4 would also escape assessment, as the total income of each of those partners is below the taxable limit. The sums paid to partners Nos. 1 and 2 would be included in their income and taxed at the rate appropriate to that income. In other words, the effect would be that, instead of Rs. 4,613 which was finally taken as the assessable income of this firm, the amount actually taxed would be Rs. 2,534. If partners Nos. 1 and 2 had no other sources of income, the effect would be that no part of the profits of this firm would be taxed at all, since those profits would be split up into five portions, each of which is less than the taxable minimum.

5. Since the Act provides for the treatment of an unregistered firm as a single unit and for the assessment of the whole of the profits of such a firm in its hands, it is reasonable to infer that the whole of the profits available for distribution to the partners, whatever form those profits may take, is intended to be taxed in the hands of the firm. It is a common arrangement of such partnerships that the whole or part of the capital invested by the partners in the business shall bear interest at a stipulated rate so that the profits earned by the firm are distributed to the partners partly in the form of interest and partly as net profits. It is, no doubt, possible for a partner—like a person not connected with the firm—to make an ordinary loan of capital on interest to the firm, and to secure that loan in the same way as an ordinary outside creditor entirely unconnected with the firm might do. It has therefore in my opinion to be determined with reference to the facts of each particular case whether the partner has made an ordinary loan of this kind, or whether he has invested further capital in the business and has stipulated, in respect of this further capital, that it shall bear interest at a specified rate. The interest on borrowed capital in the strict sense is clearly an admissible deduction in arriving at the net profits, whilst the interest on the capital (whether original or additional) invested in the business by the partners is in my opinion merely a part of the trading profits distributed in a particular way.

6. The Act has not attempted to distinguish in terms between partners' capital invested in the business with the condition that the profits shall be so distributed that the capital is considered to earn interest at a certain rate and capital borrowed in the strictest sense. Since however the assessment of the profits of an unregistered firm in its hands must rest largely on such a distinction, it is reasonable to scrutinize the Act closely in order to see whether effect has not been given to such an intention. Section 10 (2) (iii) provides that in computing the profits of a business a deduction may be made of the interest paid "in respect of

capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits.' It seems to me that the condition thus attached, namely that the payment of interest shall not in any way be dependent on the earning of profits is the means which the Act has provided for distinguishing between interest-bearing capital invested in the business and an ordinary loan of capital. The interest on an ordinary loan must be paid whatever the fortunes of the business may be, and whether profits are earned or not. The partner who invests capital however, whatever the form which that investment may take, looks to the profits of the business for the reward on his investment, and in the absence of profits no effective payment of that reward or interest can actually take place. It may be contended that section 10 (2) (iii) has reference to section 240 of the Indian Contract Act, and is merely intended to exclude the deduction of interest calculated with reference to the amount of the profits. I would however submit that the wording of the two sections is very different. The Income-tax Act insists that the payment of the interest shall be in no way dependent on the earning of profits. This is a much more forcible criterion than if it were provided that the capital must not bear interest at a rate varying with the profits. Moreover even if it were held that the legislature, in making this provision in the Income-tax Act, had in mind the provisions of section 240 of the Contract Act, it would follow that they intended to exclude the deduction of interest on capital borrowed from a person who was not a partner, but was remunerated by a share of the profits. It seems to me to follow *a fortiori* that the interest on capital invested by a partner in the business, which by its very nature is an assignation of part of the profits, is not to be deducted in computing the profits.

7. For these reasons I consider that where a partner has advanced money to a firm at a definite rate of interest, it is necessary to determine, with reference to the facts of the case, whether he has made an ordinary loan bearing interest such as any outsider might make, or whether he has invested further capital in the business on the understanding that his share of the profits will be calculated in a certain way on account of this further investment. This is in effect the question which was held by the Allahabad High Court in *In re Lalla Mal Hardeo Das*(1) to be a question of fact in each case. It remains to be seen whether the circumstances of the present case justify the finding that the partners' advances were not ordinary loans but further investments of capital in the business. The relevant circumstances in my opinion are as follows:—(i) Under the deed of partnership, two of the partners are bound to advance such sums as may be required from time to time; (ii) the firm has itself amalgamated the loan accounts of partners Nos. 1 and 2 with their capital accounts; (iii) the initial capital is Rs. 5,000, whilst the subsequent advances made by the partners amount to Rs. 67,000; and (iv) the last clause of the partnership deed provides that on the dissolution of the partnership each partner will first recoup his entire capital and then receive an equal share of the entire stock and the *ugrahi*.

Having regard to these facts I respectfully submit that there was sufficient evidence before the Income-tax Officer and the Assistant Commissioner on which they could find that the advances made by the partners were not in the nature of loans but of further investments of capital in the business.

Shamair Chand and Qabul Chand, for the Assesseees.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

The assessee in this case is a firm of Commission Agents working under the name and style of Bhola Shah Narsingh Das at Gujranwala. The firm is owned by four partners in the following shares:—Bhola Shah, Four Annas, Narsingh Das, Four Annas, Jagan Nath, Four Annas, Gian Chand, Four Annas. The firm was constituted as far back as 1919 by a deed which was registered on the 20th of July, 1919. Bhola Shah and Narsingh Das were to be the financing partners and Jagan Nath and Gian Chand the working partners. According to the deed, the capital of the firm was Rs. 5,000 which was subscribed by the first two partners in equal shares. It was provided in the deed that, if any additional sums were required for the partnership business, they shall be supplied by Bhola Shah and Narsingh Das, and, on the amounts so advanced over and above the Rs. 5,000 which was the real capital of the partnership, Bhola Shah or Narsingh Das, as the case might be, would be entitled to charge interest at the rate of Re. 0-7-6 per cent. per annum. It was also provided that, if the other two partners—Jagan Nath and Gian Chand—put in any money in the joint business, it shall also carry interest at the rate of Re. 0-7-6 per cent. per mensem. The last clause of the deed was that, in the event of dissolution of partnership, each partner would be entitled to an equal share of the stock in the shop and the outstandings after recouping the entire amount of the capital.

The firm was assessed for the year 1927-28 at Rs. 5,281 on the income for the previous year. The assessee, however, claimed a deduction of Rs. 3,762-7-3 which was the amount paid by them during the period in question to the four partners as interest on the sums advanced by them in addition to the capital which the first two of them had originally invested. The Income-tax authorities having refused to allow this deduction a petition under section 66 (3) of the Indian Income-tax Act, 1922, was made to this Court, urging that a question of law was involved on which the Commissioner should be required to state the case.

After hearing the counsel on behalf of the Commissioner of Income-tax, a Division Bench of this Court held that the question involved was one of law and it directed the Commissioner to state the case. This has now been done and we have read the statement of the case by the Commissioner and heard both counsel at length.

Before discussing the question, it is necessary to make a slight verbal correction in the question as formulated in the previous order of this Court dated the 21st of January, 1929, which has been quite rightly pointed out by the Commissioner in his statement of the case. The question, as amended, shall read as follows:—“Where a partner as partner lends money beyond the initial capital to the partnership at an agreed rate of interest and the money is used for capital expenditure, should the interest paid by the partnership to him in the ‘previous year’ be deducted in computing the profits or gains of the partnership within the meaning of section 10 (2) (iii) of the Income-tax Act?”

The decision of the question depends on the meaning to be put on clause (iii) of sub-section (2) of section 10 of the Indian Income-tax Act, 1922, which reads as follows:—“(2) Such profits or gains shall be computed after making the following allowances, namely:—(3) In respect of capital borrowed for the purpose of the business, where the payment of interest thereon is not in any way dependent on the earning of profits, the amount of the interest paid;” This identical question arose in Madras and was answered by a Full Bench of five Judges in favour of the assessee, see *Subramanian Chettiar v. Commissioner of*

Income-tax, Madras (1). In that case it was held that "when a partner generally lends money, beyond the initial capital, to the partnership at an agreed reasonable rate of interest and the money is used for capital expenditure the interest paid by the partnership to him must be deducted in computing the profits or gains of the partnership as provided by section 10 (2) (iii) of the Indian Income-tax Act." The facts of that case are on all fours with those of the present one, and the statement of the case, which has been submitted to us by the Income-tax Commissioner, Punjab, is almost in identical terms with that of the Income-tax Commissioner, Madras. Mr. Jagan Nath has attacked the accuracy of the conclusions of the Madras decision; but after hearing him at length we find no force in his arguments. We venture to think that the conclusions arrived at by the Madras Judges, as well as the reasoning on which they are based, are sound and, as we are in complete agreement with them, we do not think it necessary to repeat what has been so lucidly and elaborately stated in that judgment.

The only additional argument, which Mr. Jagan Nath put forward, is that as a partner who lends money to a partnership cannot be allowed to maintain a suit for recovery of that sum and his only remedy is to sue for dissolution of partnership, the amount so lent by him must to all intents and purposes, be considered "capital" of the partnership. We fail to see how this conclusion follows from the premises, assuming them to be correct. It seems to us that the procedure laid down for recovery of the loan does not and cannot effect the interpretation of the specific provision of the Indian Income-tax Act on which alone the decision of the present reference must depend. It is not denied that the words 'capital borrowed,' in clause (iii) of sub-section (2) of section 10 means 'money borrowed for capital expenditure of the business.' It is also conceded that the real test is whether the payment of interest on the amount advanced is or is not in any way dependent on the earning of profits. If it is so dependent, no deduction for the amount paid or payable as interest can be made; but, if such payment is not dependent on the earning of profits, it shall have to be deducted, regardless of the fact whether the advance was made by a partner or a third person. In the present case nothing has been brought to our notice to show that it falls within the first category.

The Commissioner in his statement of the case, and Mr. Jagan Nath in his arguments before us, have relied on *In the Matter of Lalla Mal Hardeo Das* (2). The facts of that case, were, however, wholly distinguishable and the question of law considered there was couched in different language. In that case the partnership was not constituted by a deed. It was admitted that no capital had been initially put into the business by any of the partners, and, after an examination of the dealings of the parties and the other circumstances of the business, it was found that the so-called advances for borrowed capital were really nothing more than capital actually and really invested in the firm. On those facts there can be no doubt that the decision arrived at was correct.

In the present case, however, the facts are wholly dissimilar. The terms on which the partnership was constituted were embodied in the deed which was duly registered as far as 1919. A certain sum of money was actually advanced by the financing partners as the 'capital' of the firm. It has not been shown that the clause relating to the payment of interest on the additional sums advanced by the partners as loan was not intended to be, or was not in fact, acted upon. The rate of interest charged is Re. 0,7-6 per cent. per mensem only. The accounts are stated to have been regularly kept and no suspicious circumstance has been brought to our notice. Emphasis has, however, been laid upon the fact that the initial capital put in by the partners was Rs. 5,000 only, while the amount

subsequently advanced by them was Rs. 67,000. In our opinion this circumstance does not prove anything against the assessee. It is worthy of note that in the Madras case, to which reference has already been made, the disparity was much greater. There the capital originally invested was Rs. 21,000, while the amount subsequently lent by the partners was over four lakhs, and it was held that this circumstance was immaterial.

We are of opinion that the question referred to us must be answered in the affirmative and the deduction claimed by the assessee should be allowed to him.

The petitioner will have his costs from the Commissioner of Income-tax, a sum of Rs. 100 deposited by him under section 66 shall also be refunded to him.

(364) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt. Chief Justice, Mr. Justice C. C. Ghose and
Mr. Justice Buckland.*

(7th April, 1930).

Kedarnath Kesariwal

... Assessee.*

v.

The Commissioner of Income-tax, Bengal

... Referring Officer.

Indian Income-tax Act (XI of 1922) Secs. 34 and 23 (4)—Assessment of escaped income—Notice calling for return given in time—Further proceedings, if limited as to time—Default in production of accounts—Assessment under Secs. 23 (4), Legality of.

Where proceedings are started under Sec. 34 of the Income-tax Act and the notice calling upon the assessee to file a return of income is given within the time limited therein, the rest of the proceedings thereunder is not further limited as to time.

Where in compliance with the notice under Sec. 34 the assessee filed a return but made default in producing account books called for under a subsequent notice, an assessment can be made under Sec. 23 (4) of the Act.

Case [Reference No. 3 of 1928] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal for the opinion of the High Court.

CASE.

In accordance with the provisions of section 66 (2) of the Income-tax Act, I have the honour to refer to the Hon'ble Court certain questions of law which have arisen out of the order passed by the Assistant Commissioner of Income-tax, Calcutta, on an appeal filed by Babu Kedar Nath Kesriwal hereinafter called the assessee against the assessment made on him by the Income-tax Officer, Calcutta District V.

2. The facts of the case are as follows:—

On the 16th March, 1925 a notice under section 22 (2) of the Act was issued on the assessee calling for a return of income in respect of the accounting year 1980-81 Dewali. On the 22nd April 1925 the return was filed showing an

* I. L. R. 58 Cal. 254 ; 34 C. W. N. 1098 ; A. I. R. (1931) Cal. 209.

income of Rs. 2,000 in round figures under the head business with remarks "Accounts have not been fully adjusted. This shall be done in as short a time as possible." Then in compliance with a notice under section 23 (2) calling for evidence on which the assessee relied in support of the return he produced accounts, which were examined by the Assistant Income-tax Officer, who reported to the Income-tax Officer that the assessee had two sources of income, *viz.*, share-brokerage and share dealing and that the assessable income was Rs. 6,921. Meanwhile the Income-tax Officer was informed that he had a much larger income since he was the proprietor of the big Jute Fatka business carried on in the name of his nephew named Dwarkadas Kesriwal. Accounts were again examined by the Assistant Income-tax Officer, who reported that no irregularity was found in the accounts. The Income-tax Officer was not however satisfied and asked the assessee to declare on affidavit that he was not the proprietor of the Jute Fatka business referred to above. The assessee did not turn up but his accountant named Sewprotap, who said he was the assessee's constituted Attorney, swore an affidavit that his master had no connection with Dwarkadas Kesriwal's firm, and that all profits earned by his master had been duly entered in the books shown. Thereupon the Income-tax Officer passed an order assessing the assessee on an income of Rs. 6,921, as reported by the Assistant Income-tax Officer, but issued a notice under section 22 (2) on Dwarkadas Kesriwal with a view to making a separate assessment on Dwarkadas Kesriwal. The notice could not be served on Dwarkadas Kesriwal as he could not be found and other people carrying on business in the building in which his place of business was, told the serving officer that Kedarnath was the proprietor of the business. Kedarnath however, refused to accept the notice as it was in the name of Dwarkadas, and declared that he had no connection with Dwarkadas. The Income-tax Officer, District IV (I) in whose jurisdiction the Fatka market was, was requested to make enquiries. These revealed the fact that Kedarnath was the real proprietor of Dwarkadas Kesriwal's business, and that the income of the business might be estimated at Rs. 25,000. The Income-tax Officer then issued a notice under section 34 asking the assessee Kedarnath Kesriwal to show cause why the assessment already made should not be reopened and also issued a notice under section 22 (4) for the production of books. The assessee's accountant appeared, denied any connection with Dwarkadas Kesriwal and did not produce any account books. An assessment was then made under section 34 on Rs. 31,921, taking the Fatka business income at Rs. 25,000 as estimated by the Income-tax Officer, District IV (I) and a penalty of Rs. 2,000 under section 28 was imposed for concealing this income.

The assessee then preferred an appeal before the Assistant Commissioner of Income-tax, Calcutta (Mr. Williams) and produced at the time of hearing of the appeal, two letters from the Secretary, Pat Association, showing that Kedarnath and Dwarkadas were separate members of the Pat Association. The Assistant Commissioner of Income-tax held that the business of Dwarkadas Kesriwal was a separately owned business and so his income should not be included in Kedarnath's assessment. He accordingly cancelled the assessment made under section 34 and the penalty imposed by the Income-tax Officer under section 28.

After the passing of the appellate order certain facts were brought to his notice by which he became convinced that in addition to the business carried on and assessed in his own name Kedarnath had several *benami* businesses, *eg.*, businesses in the name of (1) Anantaram Babulal, (2) Dwarkadas Kesriwal and (3) Anantaram Kedarnath. Besides, he had income from several heavy mortgages, which amounted to Rs. 36,000 and a house at Konnagar, and he had never shown these sources of his income in his return. He found that his own order on appeal was wrong, and, as he had no power to reverse it, he reported all the facts to the

Commissioner suggesting that the latter might review the case under section 33 or that he might proceed against the assessee under section 52 of the Act.

The Commissioner issued a notice under the proviso to section 33 asking the assessee to show cause on the 29th June 1926 why the Assistant Commissioner's order on appeal should not be cancelled, and the Income-tax Officer's order under sections 34 and 28 restored or such order passed as Commissioner thought fit. The case was then adjourned to 9th July 1926 when the assessee showed cause. He denied that he had any connection even as a partner with any business except that carried on in his own name, and suggested that a careful and searching enquiry should be made to arrive at the truth as the story about his having other sources of income was circulated by his enemies especially one by name Johurnal Khemka.

The Commissioner accordingly directed the Income-tax Officer under section 33 (2) to make a careful enquiry and report what the real income of the assessee was in the accounting year, 1925-26 (1980-81 Dewali).

In pursuance of this order the Income-tax Officer made vigorous enquiries and reported on the 9th August 1926, that Kedarnath Kesriwal is the managing member of a Hindu Undivided Family and that the share broking business carried on in his own name and alleged to be his only business, is only one of several sources of income. The income from this business alone was some Rs. 50,000 in the accounting year, viz., 1980-81 Dewali, and not Rs. 2,000 approximately as given in his return under section 22 (2). Besides this, he carried on (1) a Jute Fatka business in the name of Dwarkadas Kesriwal, the profits of which in the year in question came to Rs. 2,00,000; (2) a money lending business under the name of Anantaram Babulal, which brought in Rs. 50,000 profit; while in the same year of account he had (3) an income of Rs. 20,000 from dividends. The total income was thus reported to be Rs. 3,20,000.

After considering the Income-tax Officer's report and hearing the assessee again the Commissioner directed the Income-tax Officer to start proceedings under section 34 afresh *ab initio* to assess such income or gains as may appear from the present information or such further information as may come to light, to have escaped assessment in the original assessment made for the year 1925-26 and to impose such penalty for concealing his income as the circumstances may call for but that no assessment should be made without every reasonable effort to arrive at the truth in regard to the real amount of the assessee's income.

On the receipt of this order the Income-tax Officer issued a notice under section 34/22 (2) asking the assessee to make a full statement of his income during the year 1980-81 Dewali especially his income from interest on Hundis and income from Jute Fatka business. In compliance with this notice a return was filed on the 18th November 1926 showing an income of Rs. 2,923. The Income-tax Officer issued a notice under section 23 (2) on the same date calling for evidence in support of the return and another notice under section 28 to show cause why the assessee should not be penalized for concealing the income of the Jute Fatka business carried on in the name of Dwarkadas Kesriwal and for grossly understating his income from the share business. The accounts of 1980-81 and 1981-82 were produced and the Income-tax Officer having partly examined them found to his surprise that transactions involving crores of rupees had been carried through in the name of Dwarkadas Kesriwal, that balances had not been taken to the Profit and Loss Account, that cheques received in the name of Dwarkadas Kesriwal were always paid to Kedarnath Kesriwal's account, and

similarly that the latter paid the cheques due on the account of the former. The Income-tax Officer visited the *guddy* of the assessee and tried to examine more books there but he was not allowed to examine them; he then issued a notice under section 22 (4) calling for the books of 1979-80, the year prior to the previous year and the following papers:—

- (1) Sowda or transaction book.
- (2) Share Rokar Book.
- (3) Bank Pass Books.

Neither the accounts of 1979-80 nor the other papers specified above were produced. As a result the assessment was made under section 23 (4) on an estimated income of Rs. 3,50,048, including the income from business carried on in Dwarkadas's name. It may be that the estimate was too high as contended by the assessee, but it is practically impossible to determine now whether this is so or not. If it is, the assessee has only himself to blame as the proper materials for assessing him were not furnished.

Against the assessment the assessee filed a petition under section 27 which was rejected, and against the order of the Income-tax Officer refusing to reopen the case an appeal was filed before the Assistant Commissioner of Income-tax. At the time of the hearing of the appeal it was argued on behalf of the assessee that no proper notice under section 23 (2) was issued after the submission of the return as the notice actually issued under that section related to the assessment proceedings for 1926-27 and not 1925-26. It was worded as follows:—"To enable me to test the correctness of the return of income furnished under section 22 of the Act for the year ending 31st March 1926, I hereby require you to attend at my office, etc.....". The return in respect of the assessment proceedings for 1925-26 was for the year ending 31st March, 1925 and not 31st March 1926, and, as the assessment proceedings for 1926-27 were then also pending, the Assistant Commissioner rightly held that the assessee could safely say that he received no notice under section 23 (2) in connection with the return in question. He set aside the assessment and directed the Income-tax Officer to make a fresh assessment after issuing a notice under section 23 (2). In this appeal the question of jurisdiction, *viz.*, that the principal place of business of the assessee was not within the jurisdiction of the Income-tax Officer, District V. was first raised, but the Assistant Commissioner of Income-tax did not deal with it, probably because the point was not raised at the time of the assessment and so he had no authority to admit it in appeal.

Dissatisfied with the Assistant Commissioner's order the assessee filed a petition before the acting Commissioner for review or in the alternative for reference to the High Court of certain questions of law. He rejected the petition.

Meanwhile the Income-tax Officer issued a combined notice under sections 23 (2) and 22 (4) for production of evidence in support of the return, as directed by the Assistant Commissioner of Income-tax and of complete account books for the years 1980-81 and 1979-80 on the 3rd May, 1927. The former were produced but not the latter. At the same time the assessee filed a petition before the Income-tax Officer stating that as the assessment had been cancelled by the Assistant Commissioner of Income-tax as bad in law no fresh assessment could be made without first issuing a notice under section 22 (2). The Income-tax Officer held that as the Assistant Commissioner of Income-tax, having found that the notice under section 23 (2) was defective, set aside the assessment and direct-

ed him to start afresh from the section 23 (2) stage by issuing another notice so there was no necessity to start the preliminary proceedings all over again. The result was that an assessment under section 23 (4) was made repeating the figure of Rs. 3,50,048.

Against the assessment a petition under section 27 was filed. The objections were that no proper notices under section 34(2) and also under section 23 (2) were served and that the books of 1979-80 were missing. This last fact about the books of 1979-80 being missing was only an afterthought, as it was never mentioned before although the books were called for several times. The petition was rejected and was followed by an appeal which the Assistant Commissioner of Income-tax dismissed. In this appeal the question of jurisdiction was also raised but the Assistant Commissioner of Income-tax did not consider it as it was only raised at the appeal stage.

Objecting to the Assistant Commissioner's order an application under section 33(2) has been filed before me for review of the Assistant Commissioner's order or in the alternative for reference to the High Court of the following alleged questions of law:—

1. When the Income-tax Officer finds that an assessee has several places of business and when a question arises as to the place of assessment, can the Income-tax Officer who had been making assessments in past years, make a valid assessment in law, after such knowledge of different places of business, without any reference to his Commissioner under section 64 (3) of the Act?

2. Was the notice purported to be issued under section 34 in the case really a valid notice in law under section 34 of the Act?

Was the assessment made on the same tenable in law?

3. When the Income-tax Officer raises especially two items of income in his notice under section 34, does the Act empower him to assess other sources of income without issuing separate notices under section 34 for the same?

4. Is not the point of jurisdiction a question of law and can the same be not raised at any time?

5. Does the Act empower the Income-tax Officer to assess the income of the firm of Dwarkadas Kesriwal, the principal debtor, consisting of three different partners belonging to three different Hindu undivided families jointly with the income of Kedarnath Kesriwal, the guarantor the head of a fourth Hindu undivided family?

6. Do the facts of the case justify the Assistant Commissioner's finding that the firm of Dwarkadas Kesriwal is a *benami* business of Kedarnath Kesriwal?

7. When Dwarkadas Kesriwal appeared in person with his accounts, was the Income-tax Officer justified in making an estimate of his income without letting him know on which points the accounts were defective and why the income shown in his Profit and Loss Account should not be the basis of assessment?

8. Does the Act provide for issue of a combined notice under sections 23 (2) and 23 (4) after an assessee submits his return?

Does non-compliance in part of such a notice render him liable to an assessment under section 23 (4) depriving him of his right of appeal against the assessment?

9. Is a notice purported to be issued under section 23 (2) really a valid notice under section 23 (2) when it asks the assessee both to attend and to produce evidence instead of asking him either to attend or to produce evidence?

Is non-compliance in part of such a notice punishable with an assessment under section 23 (4) of the Act?

10. Does the language of the notice purported to be issued under section 23 (2) constitute the same as a valid notice in law asking for evidence of the section 34 return?

11. When Mr. Williams, Assistant Commissioner, arrived at the finding that the firm of Dwarkadas Kesriwal was separate from the firm of Kedarnath Kesriwal and when that finding has not been reversed by any higher authority, can the Income-tax Officer make a joint assessment for the two firms validly in law?

12. Do the facts of the case justify the Assistant Commissioner's finding that the assessee could have produced the books for 1979-80 if he wanted to do so?

13. When a section 34 assessment for 1925-26 is cancelled for illegality in the year 1927-28, whether or not the Income-tax Officer is debarred from proceeding to make a fresh assessment on account of the expiry of the time limit laid down in section 34 of the Act and whether or not the words "so far as may be" in section 34 nullify the remand order of the Assistant Commissioner under section 31 (3) (b) of the Act?

14. When an assessment proceeding is cancelled on account of illegality whether or not the force of the previous notices is spent and whether or not the Income-tax Officer must start again with the initial notice of return?

15. Is the assessment for 1925-26 doubted by the Income-tax Officer in his assessment note for the year 1926-27 and in his order under section 27 and cancelled by the Assistant Commissioner on account of illegality, is the same simply repeated by the succeeding Income-tax Officer without rhyme or reason to the best of his judgment as laid down in section 23 (4) of the Act?

16. Does the Act provide for taxation times without number of one item of income only, viz., dividends?

17. When the legality of an assessment under section 23 (4) is challenged in an appeal on various grounds is it not incumbent on the Assistant Commissioner to go into each and every one of the grounds raised and give his decision on each or he can dismiss the grounds of illegality as irrelevant or as mis-statement of facts and decide the appeal only on the point of reasonableness of the cause of prevention under section 27?

18. (a). When an assessee has submitted his return of income for 1980-81 is it legal for the Income-tax Officer to demand 1979-80 accounts in a notice under section 23 (2) or under section 22 (4) without specifying the rea-

sons for the same? (b) If the same cannot be produced for any reason is the assessment liable to be made under section 23 (4) or should the assessment be still made under section 23 (3) of the Act?

I have declined to interfere in review and decline also to refer the following questions out of those given above for the reasons given against each.

Question 1 contains a misstatement of fact. In the original assessment for 1925-26 the assessee represented his sole source of income to be share-broking and share-dealing and gave his address as 2, Royal Exchange Place (*Vide* his vokalat-nama of the 4th July, 1925, also his letter to the Income-tax Officer of the 1st February, 1926). He did not raise the question of jurisdiction at the time the assessment objected to was made. Hence no question of jurisdiction arose and the Income-tax Officer had no occasion to refer to the Commissioner under section 64 (3) of the Act.

Question 3 contains a mis-statement of fact. The Income-tax Officer asked the assessee "to make a full statement of his income during the year 1980-81, Dewali, especially his income from interest on Hundis and income from Jute Fatka business." It is thus clear that the notice covered all sources of the assessee's income. By specially mentioning 2 of the sources of income the Income-tax Officer probably meant to suggest that the income from these two sources should not be omitted from this return and he had good reasons for making this suggestion inasmuch as income from these two sources was omitted altogether from all previous returns.

Question 4.—The first part of the question, *viz.*, whether "the point of jurisdiction is a question of law" does not arise out of the Assistant Commissioner's order and it seems that circumstances may make it a question of fact or of law.

The second portion, *viz.*, whether the point of jurisdiction can be raised at any time is a question of a general nature, not strictly arising out of the Assistant Commissioner's order in the present case, and I do not think I am required to give my opinion on the question. The fact is that the question of the principal place of business was first raised in the appeal stage. As no such question was raised at the time of the assessment now objected to, the Assistant Commissioner could not go into it as it was quite a new point. Further the appeal before the Assistant Commissioner was against the Income-tax Officer's refusal to re-open the case under section 27 and the Assistant Commissioner was competent only to see if the assessee was prevented by sufficient cause from complying with all the terms of the notice issued.

Question 5.—The answer depends upon the circumstances of the cases and upon how far the statements made in this question are true. The facts stated here have not been proved and it has been found as a fact that Kedarnath Kesriwal is the proprietor of the firm known as Dwarkadas Kesriwal. Different statements, *e.g.*, (1) Kedarnath has no connection with Dwarkadas's firm, (2) Kedarnath is the guarantor of Dwarkadas's firm, go to give the lie to the facts stated in this question.

Then again the question does not arise out of the Assistant Commissioner's order.

Question 6 contains a mis-statement of fact. It cannot be said that this was the Assistant Commissioner's finding. It is only a passing remark suggesting

the reason for not producing the books. Further the Assistant Commissioner was not authorised to go into the merits of the case, the appeal being against Income-tax Officer's refusal to reopen the case under section 27.

Question 7 contains a mis-statement of fact, as in the assessment now objected to Dwarkadas did not appear in person with his accounts.

Question 11 contains a mis-statement of fact, as Mr. Williams' order referred to was in effect set aside by the Commissioner when he directed the Income-tax Officer to start section 34 proceedings afresh *ab initio*.

Question 12 is obviously a question of fact.

Question 14 contains a mis-statement of fact as the Assistant Commissioner did not cancel the proceedings but merely "set aside the assessment," a very different thing, and directed the Income-tax Officer to "make a fresh assessment by issuing a notice under section 23 (2)."

Question 15 is one of fact.

Question 16 the exact meaning of which is somewhat obscure, appears to contain a mis-statement of fact as the assessee's income from dividends was certainly not taxed more than once. Rs. 20,000 as estimated income from dividends was included in assessee's total income, but this sum was deducted in calculating his taxable income.

Questions 2, 8, 9, 10, 13, 17, and 18 appear to involve points of law and I refer them with my opinion which is as follows:—

Question 2.—It is not clear from the question itself why the notice is sought to be regarded as invalid. At the time of argument however it was explained that an ordinary notice under section 22 (2) with the addition of "under section 34" at the top was not a valid notice under section 34. The section itself does not shew that the procedure was wrong. The assessment on such a notice was therefore legal.

(At the time the notice issued there was no printed departmental form for notice under section 34 such as we have now. But this form is only an executive form and has no statutory authority behind it).

Question 8 is covered by the recent decision of the Hon'ble High Court in the case of *Harmukhrai Dulichand vs. Commissioner of Income-tax*.⁽¹⁾ The answers are:—

There is no legal objection to combining a notice under section 23 (2) and a notice under section 22 (4) in one document.

Yes. Partial non-compliance with such a combined notice renders an assessee liable to assessment under section 23 (4).

Question 9.—The notice was not produced before me and there is no office copy of the notice in the file. The order dated the 21st April, 1927 for issue of a combined notice under sections 23 (2) and 22 (4) is quite clear on the order sheet and is not defective in any way. It runs as follows:—

"Issue combined notice under sections 23 (2) and 22 (4) calling for complete account books for the years 1980-81 and 1979-80 Dewali and any other

evidence on which he may rely in support of the return. Fix 3rd May 1927 as the date of hearing."

If however, in the actual notice the superfluous words were not struck out through some clerical error, it was not a very serious defect and in any case the assessee was not prejudiced by it. In fact he understood what was meant by the notice inasmuch as he filed a petition and produced the books of 1980-81, *i.e.*, complied partly with the notice. The partial non-compliance with the notice for which the assessment was made under section 23 (4) was certainly not due to the so-called defect pointed out here.

Question 10.—The language of the question is obscure. As far as can be gathered the assessee's contention is that the form of section 23 (2) notice in a section 34 assessment should be different from the form of section 23 (2) notice in an original assessment. The law does not require this.

Question 13.—The assessment was set aside but the entire proceedings were not cancelled. The Assistant Commissioner was quite within his rights in directing the Income-tax Officer to make a fresh assessment after making such further enquiry as the Assistant Commissioner thought fit. He asked the Income-tax Officer to issue a fresh notice under section 23 (2) and make a fresh assessment. So long as the proceedings which were started in time were not entirely cancelled there was no question of time bar. The words "so far as may be" in section 34 have no bearing on the order passed by the Assistant Commissioner.

Question 17.—The appeal in question was an appeal against the Income-tax Officer's order under section 27 refusing to re-open the assessment, and the Assistant Commissioner's sole duty was to see whether the Income-tax Officer was justified in his refusal. As the assessment had been made under section 23 (4) for non-compliance with a notice under section 22 (4) the Assistant Commissioner was debarred by the proviso to section 30 (1) from considering the assessment on its merits.

Question 18.—(a) Section 22 (4) does not compel the Income-tax Officer to give the assessee his reasons for requiring him to produce accounts. The accounts required were those of the year 1979-80 Sambat, *i.e.*, those of the year prior to the previous year, so the Income-tax Officer was fully entitled to call for them; (b) before any question of law can arise in this connection the question of fact whether the assessee was really unable to produce the books of 1979-80 Dewali or not must be decided. He could not satisfy either the Income-tax Officer or the Assistant Commissioner that he could not produce them. The assessee's plea was that these books of account had been sent to his native place in Rajputana and could not be found an unlikely story in the case of such recent account books. When the Income-tax Officer paid a surprise visit to the *gadi* on the 16th December 1926 he saw a lot of account books there but the assessee would not show them to him. Later when the Assistant Commissioner was hearing the appeal against the Income-tax Officer's order refusing to reopen the assessment he asked the assessee to let him look in his *gadi* to see if these particular account books were there, but the assessee refused to agree to this. The assessee does not appear to have produced any evidence either before the Income-tax Officer or the Assistant Commissioner to prove that he was really unable to produce these books, so his assertion that they were not producible is merely an unsupported statement and improbable in itself.

Besides the 18 questions dealt with above the petitioner filed on the 15th March 1928, a supplementary list of 8 questions which he wished me to refer to the High Court. As the Assistant Commissioner's order, from which the ques-

tions are supposed to arise, was passed on the 21st September, 1927, the questions are time-barred and I have no authority to refer them.

Pugh and K. K. Chakerbutty, for the Assesseees.

The Advocate-General and R. B. Pal, for the Crown.

JUDGMENT.

RANKIN C. J.:—In this case, the Commissioner of Income-tax has referred seven questions of law at the request of the assesseees. It appears that the original notice under sub-section (2) of section 22 of the Indian Income-tax Act was served on the assesseees on the 16th of March 1925. The assesseees were required by that notice to give a return of their income for the year 1925-26—October to October—and the income of that year would be the income of the previous year 1924-25. In April 1925 they made a return and, upon this, there was an order of assessment. Sometime later, it appearing that there was a question whether the income of a certain Fatka business was or was not income belonging to the assesseees, proceedings were started by a notice under section 34 of the Act and assessment was made under section 34 of the Act by the Income-tax Officer. This assessment, however, was cancelled by the Assistant Commissioner; but the Assistant Commissioner, after he had cancelled it, apparently saw reason to think that his orders were contrary to the merits of the matter and he reported the case to the Commissioner of Income-tax for action under section 33. On the 29th June 1926, the Commissioner issued a notice under section 33 and, on the 14th September 1926, he made an order upon the Income-tax Officer to commence proceedings afresh *ab initio* by a new notice under section 34.

This new notice was served in September 1926 and it is not contended before us that the new notice served in September 1926 was beyond the time limited by section 34 of the Act. We have, therefore, to consider carefully what happened upon the basis of this notice which has never yet been set aside. On the basis of this notice, in November of that year the assesseees filed a return. Notice was issued upon them to produce certain evidence and certain books of account. They failed to comply with this notice and, consequently, on the 17th of January 1927, an assessment was made upon them on the footing that they had been in default in the matter of producing their account books—the figure upon which they were assessed being in excess of Rs. 3,00,000. Thereupon, the assesseees petitioned the Income-tax Officer under section 27 of the Act to re-open their assessment. The Income-tax Officer rejected that petition. On the 11th April 1927 they appealed from the order of the Income-tax Officer to the Assistant Commissioner and the Assistant Commissioner set aside this assessment on a sum exceeding Rs. 3,00,000. He directed the Income-tax Officer to give a new notice calling upon the assesseees to produce any evidence they had in support of their return and calling upon them to produce the account books and, he having made that order, the proceedings continued afresh in that respect.

There are two points which have been taken by Mr. Pugh from among a number of points which the Commissioner was asked to refer to this High Court. He says, first, that, if one turns to section 34 of the Act, one will find that not merely the notice parallel to the notice under sub-section (2) of section 22 must be given within the time there limited but the whole proceeding down to assessment on the alleged additional income must be completed within that time. In my judgment, the wording of the section is reasonably clear to the contrary. The wording is “the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, a notice containing all or any of the requirements which may be included in a

notice under sub-section (2) of section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section." In my judgment, the limitation, in point of time, is a limitation which applies only to the notice; and, if a notice calling upon the assessee to file a return of the additional income is given within the time therein limited, the rest of the proceedings is not further limited as to time.

The second point which Mr. Pugh has taken upon the basis of section 34 is that, under such procedure, while it may be that for failing to file a return of the additional income an assessment thereof may be made in default, the section should not be read as entailing the consequence that, if a failure is made to produce the books of account required by the authorities, an assessment can be made for a default of that character. In my opinion, the procedure under the notice referred to in section 34 is to be, as far as may be, the same as would be applied in case of an original notice under sub-section (2) of section 22. The failure to make any return at all would have to be dealt with under sub-section (4) of section 23 and I see no reason to think that the other provisions of sub-section (4) will have no effect under section 34 of the Act. In this case, one of the questions which was referred to us was question No. 13. "When a section 34 assessment for 1925-26 is cancelled for illegality in the year 1927-28, whether or not the Income-tax Officer is debarred from proceeding to make a fresh assessment on account of the expiry of the time limit laid down in section 34 of the Act and whether or not the words 'so far as may be' in section 34 nullify the remand order of the Assistant Commissioner under section 31 (3) (b) of the Act?" It is not clear what the latter portion of this question means. But, in the present case, the notice under section 34 was the new notice under section 34 and the notice on the footing of which the assessment has been made was given within the time limited by the Act. That being so, there is no want of jurisdiction by reason of the limit of time in the proceedings before us.

The first portion of the 13th question is to be answered against the assessee. The second portion I do not propose that we should answer as it is not so expressed that any answer that may be given would be intelligible.

The other questions which have been referred by the Commissioner have not been raised before us and there is no occasion to answer them.

A question, however, was intimated by Mr. Pugh as to whether or not the Income-tax Officer making the assessment in this case was the proper Income-tax Officer to deal with the matter. No such question is really raised by the Reference before us. We have dealt with it on a previous occasion and, in the present proceedings we can not deal with it at all.

The assessee must pay the costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(365) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt. Chief Justice, Mr. Justice C. C. Ghose
and Mr. Justice Buckland.*

(7th April, 1930).

Protap Chandra Ganguly

.. Assessee.

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Indian Income-tax Act (XI of 1922) Secs. 23 (4), 27, 29 and 30—Non-submission of return and assessment under Sec. 23 (4)—Issue of mistaken demand notice—Second proper demand notice, legality of—Appeal against order refusing to re-open assessment—Scope and limits of jurisdiction.

Where a notice of demand issued on the basis of an order of assessment under Sec. 23 (4) for failure to submit a return did not make it clear that the assessment had been made in default of filing a return, a fresh notice of demand issued after cancelling the first mistaken notice is legal.

In an appeal from an order under Sec. 27 of the Income-tax Act refusing to re-open an assessment the Assistant Commissioner is not bound to deal with the merits of the assessment, the only question before him being whether there was not sufficient cause for re-opening the assessment.

Case [Reference No. 11 of 1928] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal for the opinion of the High Court.

CASE.

In accordance with the provisions of section 66 (2) of the Income-tax Act XI of 1922, I have the honour to refer to the Hon'ble High Court certain questions of law arising out of the order of the Assistant Commissioner, Calcutta on the appeal filed by the assessee, Babu Protap Chandra Ganguli, against the assessment made on him for the year 1927-28.

2. The following are the facts of the case: Babu Protap Chandra Ganguli, hereinafter called the "Assessee," is carrying on business at 16, Bridge Road, Chetla, Calcutta. Besides business he has other sources of income, viz., dividends, interest on securities, property and as a commission agent. His previous year is the Bengali year. On the 14th April 1927 a notice was issued upon him under section 22 (2) of the Income-tax Act calling for a return of his income during the previous year, 1333 B.S., by the 2nd June, 1927. No return was filed on the due date, nor was any application for extension of time for the submission of the return made on the due date. The Income-tax Officer however, waited till 4th June, 1927, when the assessee filed an application through his pleader for time till 4th August 1927. Time was granted till 25th July 1927 but still no return was filed. On the 27th July 1927 the pleader of the assessee appeared before the Income-tax Officer and said that as he had had to leave Calcutta he could not submit the return. The Income-tax Officer at once pointed out to him that he could not wait and must finish the assessment that day. Accordingly on the 27th July 1927 the Income-tax Officer assessed the assessee on an income of Rs. 54,260, under section 23 (4), and on the next day the usual notice of demand under sec-

tion 29 issued. On this day the assessee submitted the return but no action could be taken on this as the assessment had been completed on the previous day. Subsequently on the 1st August 1927 the Income-tax Officer found that a clerical mistake had crept into the notice of demand as the top alternative in line 8 of paragraph 5 was penned through. So he issued another notice of demand cancelling the original notice.

On the 1st August 1927 the assessee submitted a petition under section 27, but no action was taken on this as the 2nd notice of demand had issued on that day. On receipt of the 2nd notice of demand on 6th August 1927 the assessee filed another petition under section 27 to reopen the assessment on the ground that his pleader had been too busy to submit the return in due time. The Income-tax Officer rejected the petition as the cause shown was very weak.

Objecting to the order of the Income-tax Officer the assessee filed an appeal before the Assistant Commissioner, Calcutta, who upheld the Income-tax Officer's order refusing to reopen the assessment.

I am now asked, in the event of my declining to interfere in review, to refer the following questions of law to the Hon'ble High Court.

- (A). Whether the second notice of demand was a legal one?
- (B). Whether in the circumstances of the case the petitioner was deprived of his rights under section 22 (3)?
- (C). Whether an assessment under section 23 (4) deprived the petitioner of his claims based on the previous undertaking of the Income-tax Officer, with respect to the bad debts account of Rai Charan Rahut?
- (D). Whether the Assistant Commissioner of Income-tax should have considered paragraph 6 of the statement of facts submitted to him?
- (E). Whether the petitioner is entitled to the advantages of the usual interpretation of the words "Sufficient cause," in view of the fact that the return was delivered in good faith to your petitioner's pleader for submission by the due date?

Out of these five questions of law questions B, C and E cannot be referred to the High Court for the reasons given against each below.—

It is difficult to understand what exactly question B means. There was nothing to prevent the assessee from filing a return at any time before the assessment was made but he did not file it till the day after the assessment was made. In any case this appears to be a question of fact.

Question C.—This question is based upon a mis-statement of fact as the Income-tax Officer did not give any undertaking to write off bad debts in the name of Rai Charan Rahut at the time of the assessment for 1926-27. Moreover, this question does not arise out of the Assistant Commissioner's order on appeal.

Question E is a pure question of fact.

I refer therefore questions A and D. My opinion on these two questions is as follows:—

- (i). The issue of a second notice of demand in the circumstances referred to above is quite legal, and the assessee has not quoted any section of the law to show that the issue of such second notice is illegal. Further a mistake in a notice of demand does not affect the validity of the assessment.
- (ii). Paragraph 6 of the statement of facts attached to the appeal petition deals with the merits of the assessment. But as the appeal in this case was against the Income-tax Officer's order under section 27 refusing to reopen the assessment all that the Assistant Commissioner was concerned with was to see whether the assessee was or was not prevented by sufficient cause from making a return. He was debarred from going into the merits of the assessment.

JUDGMENT.

RANKIN, C. J.:—The assessee in this case received a notice under subsection (2) of section 22 of the Indian Income-tax Act requiring him to lodge a return of his income by the 2nd of June 1927. No return was filed by that date; but, on the 4th of June, the assessee filed an application through his pleader asking the Income-tax Officer to give him time till the 4th of August. The Income-tax Officer gave him time till the 25th of July and, on the 25th of July, the assessee failed to file any return. Two days later—on the 27th of July, his pleader appeared before the Income-tax Officer and said that, as he had to leave Calcutta, he could not submit his return. The Income-tax Officer said that he could not wait and must finish the assessment there and then. Further adjournment was, therefore, refused. On that date, an assessment was made by the Income-tax Officer under clause (4) of section 23 in default of the filing of return. It is quite clear under the Income-tax Act that, although an assessee is late in filing his return, nevertheless if he does file it before the assessment is actually made the return has to be considered and dealt with although out of time.

In this case, however, the assessment was made within the meaning of subsection (4) of section 23 on the 27th of July by which time no return had been filed. On the next day, the assessee came along with his return; but no action could be taken upon that as an order of assessment upon a different basis altogether had already been made. A notice of demand was issued upon the basis of the order of assessment and this notice of demand appears to be inaccurate in respect that it did not make clear that the assessment had been made in default of filing a return as distinct from certain other defaults. However, that notice of demand operated nothing. It was cancelled and a fresh notice issued. A demand notice to an assessee is simply a notice which apprises him of the previous fact, namely, that he had been assessed at a certain amount.

In this position, the assessee submitted several petitions; but, in particular, he appears to have submitted an application before the Income-tax Officer under section 27. It was quite open to the Income-tax Officer to entertain the application showing that the delay in filing the return was due to sufficient cause and that the assessee should be given the benefit of an order cancelling the assessment of the 27th of July and directing the assessment to be reopened. The Income-tax Officer, however, dealt with that matter on the facts, found no sufficient cause and rejected the application. From this order, an appeal was taken to the

Assistant Commissioner. The Assistant Commissioner being of opinion that there was no sufficient cause simply dismissed the appeal. Then the matter was taken to the Commissioner and the Commissioner took the same view that the pleader's negligence was no sufficient cause; but, being asked to refer certain questions of law to this High Court, he has referred two. We are not concerned with the questions which he has not referred.

The first question is whether the second notice of demand was a legal one. The answer to that is that there can be no objection whatever to it. There was a perfectly good assessment order on the 27th July and the fact that a mistaken notice was sent to the assessee in no way prevents a proper notice being sent when the mistake was discovered.

The second question which has been referred to us is whether the Assistant Commissioner of Income-tax should have considered paragraph 6 of the statement of facts submitted to him. The meaning of that question is whether the Assistant Commissioner on an appeal from an order refusing to re-open the assessment under section 27 was obliged to enter into the merits of the assessee's return—his actual position whether as a member of an undivided Hindu family or otherwise. The Income-tax Commissioner says that the only question before the Assistant Commissioner was whether the assessment should be re-opened—the order dated the 27th July set aside and the assessment re-opened. In my opinion, the Commissioner's view is perfectly right. He having decided that there was no sufficient cause for re-opening the assessment, the assessment order stood and there was nothing then to enquire about.

In my opinion, therefore, the two questions referred to us should be answered in favour of the Income-tax authorities and against the assessee.

The assessee must pay the costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(366) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Horace Owen Compton Beasley, Kt., Chief Justice, Mr. Justice Anantakrishna Ayyar and Mr. Justice Cargenven.

(11th April, 1930).

T. Manavedan Tirumalpad, Senior Raja of Nilambur . . . Assessee.*

v.

The Commissioner of Income-tax, Madras . . . Referring Officer.

Indian Income-tax Act (XI of 1922)—Unassessed forest lands—Income from sale of timber—Assessability to income-tax.

Sums received by sale of timber trees on unassessed forest lands are income chargeable to income-tax.

Case [O. P. No. 152 of 1929] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the High Court under section 66 (2) of the Income-tax Act, (XI-22).

2. The petitioner who is the owner of extensive unsurveyed and un-assessed forest lands in Malabar and the Nilgiris was assessed for the year, 1928-29, by the Income-tax Officer, Palghat, on an income of Rs. 5,395, from property and Rs. 3,07,629 income from fees received in respect of timber cut and removed from the forests and other miscellaneous receipts. This sum of Rs. 3,07,629 was wrongly classified by the Income-tax Officer under the head "other sources." The greater part of the income which relates to fees for timber felled and removed and profits from sale of elephants should have been classified under the head "business." In computing the income of Rs. 3,07,629 the Income-tax Officer included a sum of Rs. 1,19,098 claimed as a deduction by the petitioner as being a receipt of a capital nature. This sum is said to represent the estimated capital value of the timber cut and removed from the petitioner's forest in return for which he received certain "kuttikanom" fees. The petitioner contended that by the sale of the timber in the forest he was practically converting a good portion of the capital into cash and that to the extent of the sum of Rs. 1,19,098 (50 per cent. of the Kuttikonam fees) the receipts from Kuttikonam fees should be regarded as receipts of a capital nature. The Income-tax Officer declined to accept this contention and disallowed the claim. The petitioners thereupon appealed to the Assistant Commissioner but without success. An extract from the Assistant Commissioner's order is filed Exhibit A.

3. The petitioner has now applied to me to refer for the decision of the High Court the following question of law, *viz.* "Whether the amounts received by sale of timber trees are income, liable as such to income-tax." The petitioner is conducting a business in the sale of forest produce. He does not sell the land with the produce growing on it. He sells only the produce of the forest or that which the forest yields. His business is of the same nature as that carried on by a person working a mine or a quarry. The petitioner's claim in this instance amounts to one for an allowance for the exhaustion of capital. It is a well established principle of Income-tax law that for the purposes of taxation no deduction can be made from profits for the exhaustion of capital. There is nothing peculiar to this case to distinguish it from other decided cases in which this principle has been applied. I would therefore ask your Lordships to answer the question propounded in the affirmative.

EXHIBIT A.

4. *Income received from Kuttikonam.* Rs. 1,19,098. It was explained to me by the appellant's advocates that Kuttikonam meant the fees paid by people for the right to remove trees from the forests. The contention is that these fees do not represent income in the hands of the appellant; but realisation of capital—the argument being that as the trees are cut so the capital is exhausted. What the appellants really claim is what has never so far been allowed under the Indian Income-tax Law, namely, an allowance for exhaustion of capital. It has always been the law in India not to give any allowance for wasting assets, or for the amortisation of the capital value of an asset, or for the exhaustion of capital, except where depreciation is specifically provided for as in the case of machinery and plant. Whether one is dealing with quarries or with mines or with forests, the principle is the same—the law provides no allowance for wasting assets or exhaustion of capital.

There is a very feeble attempt made in the grounds of appeal to urge that in taxing the fees received for the right to remove timber we are taxing agricultural income. I refer to the following contention contained in the grounds of appeal: "The Income-tax Officer ought to have held that the Income-tax Act was never intended to cover any income from trees or forests on one's own land, and it is an undisputed fact that petitioner's forests are all his Jenmam property." Agricultural income is exempt from taxation under the Act only if it is derived from land which is used for agricultural purposes, and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of Government as such. In the present case the land on which the timber grows is not assessed to land revenue and is not subject to a local rate assessed and collected by officers of Government.

T. R. Venkatarama Sastri, and T. B. Balagopal, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question referred to us by the Commissioner of Income-tax is, "Whether the amounts received by sale of timber trees are income, liable as such to income-tax."

The assessee is the owner of unassessed forest lands in Malabar and was assessed by the Income-tax Officer, Palghat, for the year 1928-29 on an income of Rs. 5,395 from property and Rs. 3,07,629 from fees received in respect of timber cut and removed from the forests and other miscellaneous receipts. The assessee objects to the latter assessment. Before the Commissioner his contention was that he had purchased the forests with trees growing therein and that as the trees were cut down and carried away the capital was thereby decreased. The Commissioner of Income-tax has pointed out that similar circumstances exist in the case of mines and quarries—this is conceded by Mr. Venkatarama Sastri who appears for the assessee—and that in neither of those cases is any deduction allowed by reason of the fact that as years go on the amount of coal under the land in the case of the mines is diminished and the amount of the stones to be quarried in the case of the quarry is diminished. Similar views have been taken in the English Courts with regard to minerals.

Mr. Venkatarama Sastri here argues that this is not to be treated as assessable income at all although he admits that he can see no difference between the income derived from the sale of coal and the sale of stone quarried in a quarry or from income derived from the sale of paddy grown on land. Of course we are unable to distinguish between the income derived from the sale of paddy which is grown on land and the income derived from the sale of timber cut in a forest; but the profits earned from the sale of paddy would be assessable to income-tax but for the special exemption given to that income in the Income-tax Act by reason of its being agricultural income. There is no such exemption in the case of income derived from the sale of timber. Under the circumstances, we answer the question referred to us in the affirmative. The assessee will pay Rs. 250 costs to the Commissioner of Income-tax.

(367) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Horace Owen Compton Beasley, Kt., Chief Justice, Mr. Justice Anantakrishna Ayyar and Mr. Justice Curgenvven.

[11th April 1930]

S. M. P. Periasamy Nadar and Company .. Assessee.*
v.

The Commissioner of Income-tax, Madras.

Indian Income-tax Act (XI of 1922), Secs. 10 (2) (iii) and 66 (3)—Unregistered firm—No pre-partnership agreement to contribute further capital at agreed rate of interest—Interest payments to partners—Finding against loans by partners—Deductability of interest.

Where there was no specific agreement between the partners prior to the starting of the partnership business, specifying the amount of initial capital contributed by each of the partners and providing for contribution of further capital at an agreed rate of interest and the Income-tax authorities found that the amounts standing to their credit in the firm's accounts were not loans, sums paid to them as interest on those amounts are not deductible under Sec. 10 (2) (iii) of the Income-tax Act in the computation of the profits of the firm.

Application [O. P. No. 179 of 1929], under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922), for an order to direct the Commissioner of Income-tax, Madras, to state a case for the opinion of the High Court.

Commissioner's Order under Section 66 (2).

This is the case of an unregistered firm consisting of V. P. Periaswami Nadar, P. P. Sivanandi Nadar and K. P. M. Shanmuga Nadar, who are petitioners. The firm was assessed for the year 1928-29 on an income of Rs. 25,905 by the Income-tax Officer, Virudhunagar. In computing the profits the Income-tax Officer, disallowed three sums aggregated to Rs. 7,633-4-0 being the interest paid to the three partners, on the ground that these sums represented interest paid on the capital of the partners and not interest paid by the firm on any 'loan'. In its appeal to the Assistant Commissioner against the assessment the firm contended that the sums standing to the credit of the partners' accounts represented loans made by them to the partnership. Attention was also drawn to the fact that there was a sum of Rs. 38,993 standing at the credit of the Bad Debts Reserve Fund account on which no interest was charged. In disposing of the appeal the Assistant Commissioner reduced the total taxable income of the firm to Rs. 25,820 but did not alter the assessment, so far as the disallowance of the sum of Rs. 7,633-4-0 was concerned. The petitioners have now asked me to refer to the High Court under section 66 (2) the following questions alleged to be questions of law arising out of the order of the Assistant Commissioner:—

1. Whether under the circumstances stated above, the amount of Rs. 38,993 is the capital of the petitioners' partnership.
2. Whether interest payments made to partners in cases of firms which have no subscribed capital would be admissible charges under section 10 (2) (iii) of the Act.

* (1930) 59 M.L.J. 778 ; 32 L. W. 935 ; A. I. R. (1930) Mad.1003.

3. Whether interest payments made to the partners of the petitioners' firm, under the circumstances mentioned in the petition and in the order of the Assistant Commissioner of Income-tax are admissible items of expenditure under section 10 (2) (iii).

The only question which arises in this case is whether there was a legal loan to the firm by the partners. This question is clearly one of fact. The books do not show any account for capital other than the accounts standing in the names of the three partners. There is no agreement either defining the capital to be subscribed by the partners, or setting out the manner in which loans are to be raised, or laying down the terms on which the alleged loans have been advanced. On the other hand there is the fact that the amounts to the credit of the three partners stand in ledger folios headed "*Mothalvaravu*" account. The petitioners, however, contend that these amounts represent loans made by the partners to the business and do not constitute the capital of the business and in support of this claim they adduce the following arguments: (1) that it is possible to carry on a thriving business without capital and the nature of their business was such that no initial capital was necessary, (2) that if any amount has to be treated as the capital it should be the sum of Rs. 38,993 at credit of the Bad Debts Reserve Fund account, (3) that no weight attaches to the heading "*Muthalvaravu*" in the ledger folios, the correct equivalent of "capital" being "*Moolathanam*", and that therefore the sums in question are not capital, (4) that, in the alternative, they should be held to be borrowed capital, and (5) that the fact that interest is paid on the amounts in question is itself evidence of a loan.

It is no doubt possible in certain cases to carry on business entirely on borrowed capital, but in such cases it has to be proved that the capital employed is really borrowed capital and the question whether the capital is "borrowed" or not is purely a question of fact. In the present case, it has not been admitted by the Income-tax authorities that the petitioners' business needs no capital.

As regards the reserve for bad debts, I hold that this has been formed for the purposes which the name indicates and I find that it had undoubtedly been utilised for that purpose. It is to all intents and purposes a reserve fund and can in no sense therefore be regarded as subscribed capital and it has not been admitted by the Income-tax authorities that the amount of this fund is the capital or part of the capital of the business. The elaborate explanation that has been given regarding the Tamil equivalent of 'capital' has no force. It is well known that the word "*Muthalvaravu*" is the term invariably adopted in Tamil accounts to represent capital. The final argument which is relied on as proof that the amounts in question are 'loans' is that interest has been adjusted on these amounts. This, in my opinion, is no evidence that the amounts represent loans. The adjustment is no more than an arrangement adopted, in view of the fluctuating nature of the amount of capital advanced by the partners, to secure an appropriate variation of the shares of the three partners in the profits of the firm. I consider, therefore, that the authorities below rightly held that the petitioners have not proved the existence of a legal loan. On this finding no question of law arises. I therefore dismiss the application.

K. V. Sesha Ayyangar, for the Assesseees.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE:—On this petition we are asked to direct the Commissioner of Income-tax to refer the following question: "Whether interest

payments made to partners of the petitioners' firm under the circumstances mentioned in the petition and in the order of the Assistant Commissioner of Income-tax, are admissible items of expenditure under section 10 (2) (iii) of the Indian Income-tax Act".

The assessee is a partnership firm carrying on business in the purchase and sale of cotton seeds and it appears now to be a very flourishing business. In the year of assessment, 1928-1929, it was assessed to income-tax in the amount of Rs. 25,095. In arriving at this assessment, the Income-tax Officer disallowed a sum of Rs. 7,633-4-0 which the assessee claimed to be entitled to a deduction of from the gross profits of the partnership. They based their claim, as is apparent from the question we are asked to direct the Commissioner of Income-tax to refer, on section 10 (2) (iii) of the Indian Income-tax Act. That section allows deduction "in respect of capital borrowed for the purposes of the business where the payment of interest thereon is not in any way dependent upon the earning of profits, the amount of interest paid". It was contended by the assessee that this sum of money was interest on capital borrowed from, or at least a loan to the partnership by the individual partners and as such not assessable to income-tax.

In this connection much reliance was placed by Mr. K. V. Sesha Ayyangar on the Full Bench decision in *Subramanyam Chettiar v. Commissioner of Income-tax, Madras* (1). There a Full Bench of which I was a member held that where a partner genuinely lends money, beyond the initial capital, to the partnership at an agreed reasonable rate of interest and the money is used for capital expenditure, the interest paid by the partnership to him in the year of assessment must be deducted in computing the profits or gains of the partnership as provided by section 10 (2) (iii) of the Indian Income-tax Act. That is all that that case decides; and when the facts of the case are looked into, it will be seen that before the partnership started, there was an agreement in which the amount of capital contributed by each of the partners was set out and the rate of interest agreed to be paid upon the capital so contributed was also agreed upon. In this case there is no such agreement. Further more, in the agreement in that case there was a provision that after the partnership started working, the partners might contribute further capital to the partnership and that if they did so, they should receive interest at a certain rate on the capital so contributed. That case in no way, in our view, supports the contention of Mr. Sesha Ayyangar. There is no agreement whatever in the present case to contribute any capital, or lend any monies, nor is there an agreement to pay any interest.

It is contended by the assessee that when the partnership started the business, the business was a very small one and that there was no initial capital. But it is quite obvious, as the Assistant Commissioner of Income-tax says in his order, that a business with so large a turnover as this one could not possibly be conducted without some capital and that what happened in this case was that a certain amount of the profits earned by the partnership were allowed to remain in the partnership as capital by means of which to carry on the partnership. This is a very different case to the Full Bench case where there was a specific agreement to contribute further capital beyond the initial capital already contributed.

There is a further difficulty in the way of Mr. Sesha Ayyangar namely, that whereas in the Full Bench case there was an agreement to pay a fixed rate of interest, here, as I have already stated, there is no agreement to pay any

interest at all. But as a fact it does appear that for a period of 17 years 12 per cent. interest was paid on the amounts allowed to remain in the partnership by the partners and it is therefore quite obvious that in those years the partnership earned sufficient profits to enable the partnership to pay that high rate of interest. It must also be equally clear that had there been no such profits, no such rate of interest could have been paid. Therefore, the payment of interest was dependent on the earning of profits. There is not, as in the Full Bench case, a definite and an enforceable agreement to pay interest. What was strenuously argued before us in that case, so far as my recollection serves me, was that, quite irrespective of any profits being earned, the rate of interest agreed upon was payable. Mr. Sesha Ayyangar is, therefore, unable to bring himself within the provisions of section 10 (2) (iii) of the Indian Income-tax Act.

Another matter which I think I ought to mention is that 'Unruvenkatachariar, J who was a member of that Full Bench in his answer to the question referred stated that this question is purely a question of fact, and with that statement I am inclined to agree.

Under these circumstances, we decline to direct the Commissioner of Income-tax to refer this case. The assessee will pay Rs. 150 costs to the Commissioner.

(369) IN THE HIGH COURT OF JUDICATURE AT MADRAS.

Before Sir Horace Owen Compton Beasley, Kt., Chief Justice, Mr. Justice Anantakrishna Ayyar and Mr. Justice Curgenvven.

(14th April, 1930).

K. P. Muhammad Kassim Rowther

.. Assessee*

v.

The Commissioner of Income-tax, Madras

.. Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 22 (4) and 23 (4)—Assessee owning major share in foreign business.—Notice to produce foreign accounts, Legality of—Asst. under Sec. 23 (4)—Scope and limits of Income-tax Officer's power.

The assessee, a resident of British India with four-fifth share in a business carried on in Penang with a non-resident, was required by the Income-tax Officer under Sec. 22 (4) of the Income-tax Act to produce all the original accounts of the Penang business. On non-compliance with the requisition an assessment was made under Sec. 23 (4), the alleged refusal of the non-resident partner to produce the accounts not having been believed in by the Officer. On a reference to the High Court,

HELD (1) *that the Income-tax Officer was entitled to require the production of the accounts of the foreign business which would be relevant for determining the quantum of profits made there; and*

(2) *that on the finding that the accounts called for were under the control of the assessee who could have produced them, the assessment was legal.*

* (1930) 59 M. L. J. 220; 52 L. W. 165; A. I. R. (1930) Mad. 763.

An assessee called upon to produce accounts ordinarily in his possession and control must show that he was incapable of producing them; while the onus would be on the Income-tax Officer to show that the assessee could produce accounts not ordinarily in his possession and control but failed to do so.

Case (O. P. No. 145 of 1929) stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Madras, in compliance with the order of the High Court dated 11th October, 1929.

CASE.

In accordance with the High Court's order quoted above I have the honour to refer the following case for the opinion of the Hon'ble the Judges of the High Court under section 66 (3).

2. The petitioner is a resident of Kondagai within the jurisdiction of the Income-tax Officer, Negapatam. He owns lands and house properties in British India and is a partner owning a 4/5th share in a firm carrying on business in cloth and rubber in Penang in the Federated Malay States.

3. The deed of partnership under which this business is carried on reserves to each partner the right of free access to the accounts and the right to inspect and copy them.

4. For the assessment of the year 1928-29 the petitioner was called on to make a return of his income in the prescribed form. He returned the form sent to him without entering any figures in it. But on the form was written in Tamil: "No interest income or business". The Income-tax Officer called on the petitioner by a notice under sections 22 (4) and 23 (2) to adduce evidence in support of his return and to produce certain accounts and documents. In response to this notice the petitioner's authorised agent appeared but did not produce any evidence. The Income-tax Officer had reason to believe that the petitioner had been receiving remittances from his business abroad. He therefore required him again by a notice issued under section 22(4) of the Income-tax Act to produce the accounts relating to the cloth business at Penang and the rubber estates at Parlis in the Federated Malay States for the years, 1925-26 to 1927-28. This notice was accompanied by a covering letter dated 3rd September, 1928 of which I enclose a copy—Exhibit A.* The petitioner did not produce the accounts but stated that the business in the Federated Malay States was a partnership concern and that as the account books were the property of the partnership he was unable to produce them. As the petitioner had not produced any of the accounts specified in the notice, the Income-tax Officer held that he had failed to comply with the notice under section 22(4) and accordingly made an assessment on the petitioner under section 23(4) on an income of Rs. 1,00,133 as under:

Property	..	Rs.	133
Foreign profits received in British India	..	Rs.	1,00,000
			<hr/>
			1,00,133
			<hr/>

5. The petitioner applied to the Income-tax Officer under section 27 for a re-opening of the assessment, but the Income-tax Officer declined to re-open the assessment as he was not satisfied that the petitioner had been prevented by sufficient cause from complying with the notice under section 22(4). A copy of the order giving reasons for this decision is enclosed—Exhibit B.*

* Not printed.

6. The petitioner appealed to the Assistant Commissioner against the Income-tax Officer's order. Though the question before the Assistant Commissioner was merely whether the petitioner had or had not been prevented by sufficient cause from complying with the notice issued to him by the Income-tax Officer for the production of the foreign accounts, he allowed the petitioner even at that stage a further opportunity of producing evidence. He suggested that copies should be made from the daybooks in Penang relating to the year 1927-28, and the petitioner gave a written undertaking dated 18th December, 1928, to do so. A copy of this is enclosed—Exhibit C.* On March 5th, 1929, he produced an extract of his personal ledger taken from the books of the Penang firm and along with this presented a petition a copy of which is enclosed—Exhibit D.* The extract showed that he had received Rs. 5,000 in Madras in return for a cheque drawn upon his Penang business. In the absence of fuller evidence the Assistant Commissioner was not prepared to believe that this was the only remittance. As even at this stage the petitioner had not produced either the accounts or copies of them (apart from the extract above mentioned) the Assistant Commissioner dismissed the appeal.

7. The petitioner then applied to my predecessor for a reference to the High Court on two alleged questions of law said to arise out of the Assistant Commissioner's order. My predecessor declined to make a reference.

8. On the petitioner's application to the High Court, the Court has now ordered me to refer the following two questions for its opinion and I accordingly refer them.

Question (1). "Whether on the facts found in this case it is open to the Income-tax authorities to require the petitioner who is assessed under section 23(4) to produce all the original accounts of the firm carrying on business outside British India".

Question (2). "Whether it is open to the authorities to require copies of the whole accounts to be produced."

9. My opinion on these questions is as follows:—

Question (1). The provision of law empowering the Income-tax Officer to require the production of accounts is section 22 (4). The power is conferred subject to two restrictions (i) that the person required to produce the accounts must be a person upon whom a notice under section 22 (2) has been served; and (ii) that accounts relating to a period more than 3 years prior to the previous year may not be called for. Subject to these restrictions an Income-tax Officer may require the production of any accounts. The profits of a foreign business are liable to tax if remitted—section 4 (2)—and the accounts of such a business are evidence both of the amount of the profits and of the fact of remittance. I consider, therefore, that it was open to the Income-tax Officer to call for the foreign accounts in this case.

The fact that the accounts were in this instance those of a partnership does not appear to alter the legal position. The petitioner was the dominant partner with a 4/5th share in the firm. The accounts, if not in his physical possession, were certainly under his control. He had the right to inspect and copy them. His statement that in the matter of their production he was overruled by his partner was rightly disbelieved, and even if true would not justify his failure to comply with the notice.

* Not printed.

Question (2). The formal ground on which assessment was made under section 23(4) in this case was the petitioner's failure to respond to a notice calling for the original accounts. It was made clear that other evidence, such as daybook extracts or copies, if in existence, would be considered, but nothing turns on that. Petitioner was not assessed under section 23(4) for failure to produce "copies of the whole accounts", and I submit therefore that this question is one which on the facts of the case does not arise. But it is clear that copies of the accounts, if in existence, are documents which can be called for under section 22(4), which does not relate to accounts alone.

T. V. Muthukrishna Aiyar, M. Subbaraya Aiyar and N. Muthuswami Aiyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

The question referred to us by the Commissioner of Income-tax is as follows: "Whether on the facts found in this case it is open to the Income-tax authorities to require the petitioner who is assessed under section 23(4) to produce all the original accounts of the firm carrying on business outside British India."

The facts of the case are that the assessee who resides in British India carries on business in Penang in partnership with another who is in Penang and that in respect of the partnership the assessee is entitled to a four-fifth share and the other partner in Penang to one-fifth share. The Income-tax Officer called upon the assessee to produce all his accounts books, day books, ledgers, etc., of the Penang business. The assessee did not comply with the request. Before the Income-tax Officer he stated his inability to do so and he produced before him his one-fifth sharer who stated that he was unwilling that the assessee should produce the Penang account books. It is quite clear on reading the order of the Income-tax Officer—and it is definitely so stated in the order of the Commissioner of Income-tax—that this story was not believed by the Income-tax Officer and certainly, having regard to the fact that in this partnership he is a four-fifth sharer, it does not seem to us to be at all likely that the one-fifth sharer would have refused to produce the Penang account books if his partner had so requested. The whole story sounds a most improbable one and we think that the Commissioner of Income-tax has taken up the correct position in disbelieving the story.

The question to be considered here is, first of all, whether when a foreign business is carried on by an assessee in British India, the Income-tax Officer is entitled to require the assessee to produce the books of his foreign business. On this point we are clearly of the opinion that the Income-tax Officer is entitled to do so.

The next point that arises is, what account books is he entitled to call upon the assessee to produce? The answer to this question obviously must be such account books as are necessary to enable the Income-tax Officer here either to check the return already made by the assessee, or himself to form an estimate of the income of the assessee. In this case it is conceded by the assessee that the Penang books were relevant. Obviously they were because one of the things the Income-tax Officer has to consider was whether the remittances from Penang to British India came out of capital, or whether they came out of profits made in the Penang business. If there were profits of an amount sufficient to

enable the remittances to be made to British India, then the inference is that the remittances came out of profits. So the first thing the Income-tax Officer had to consider was whether any profits and, if so, to what amount had been made in Penang. Clearly for the purpose of deciding that question he had to have inspection of the Penang account books and by Penang account books we mean not only the ledger but also the cash and the day books.

The other question arising is whether, if the assessee does not produce the account books, the Income-tax Officer is entitled under all circumstances to make the assessment under section 23(4) of the Indian Income-tax Act. We think that it has got to be shown that the assessee could comply with the order for the production of the account books. It clearly would not be right to say that the Income-tax Officer is entitled to call upon a person to produce account books which would not ordinarily be in the possession and control of that person. We think that the right view to take of the case is that where an Income-tax Officer calls upon an assessee to produce account books which ordinarily would be in his possession and control, then the assessee has got to show that he is incapable of producing them. Of course, if the Income-tax Officer calls upon an assessee to produce account books which would not ordinarily be in his possession and control, then the onus would lie upon the Income-tax Officer of showing that the assessee could produce them but has failed to do so. In this case, for the reasons we have already stated, it is quite clear that the books were under the control of the assessee, that he could have produced them and that he failed to comply with the notice issued to him to produce them. Under these circumstances, the Income-tax Officer was quite entitled to make the assessment under section 23(4) of the Indian Income-tax Act. The question referred to us is answered accordingly. The assessee will pay Rs. 250 costs to the Commissioner of Income-tax.

(370) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Mr. Justice Tek Chand and Mr. Justice Aga Haider.

(24th April, 1930).

Harkishan Lal

v.

.. Assessee.*

The Commissioner of Income-tax, Punjab
and N. W. F. Provinces

.. Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 4 (2) and 10 (2) (iii)—Foreign business—Interest paid on capital therefor—If allowable against profits brought into British India.

Interest paid in the accounting year in British India on capital borrowed here for a business outside British India is a permissible allowance under Sec. 10(2) (iii) of the Income-tax Act against the profits of that business assessed under Sec. 4 (2), if the profits brought into British India in the accounting year are in excess of the interest paid, though all the profits of the business earned in the account year and the three preceding years have not been brought into British India.

* A. I. R. (1930) Lab. 982.

Case (Civil Reference No. 31 of 1929) stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Punjab and N. W. Frontier Provinces in compliance with the order of the High Court, dated 5th April, 1929.

CASE.

In pursuance of the order of the High Court, dated 5th April, 1929, I have the honour to refer the following case for the opinion of the High Court under section 66(3) of the Indian Income-tax Act, 1922.

2. *Facts of the case.* The petitioner L. Harkishan Lal, in addition to his activities as the Managing Director or Director of various joint stock companies, is also the owner of other businesses one of which, the Bhupindra Flour Mills, is situated in Bhatinda in the Patiala State outside British India. In the assessment for the year 1925-26 a sum of Rs. 1,95,000, subsequently reduced in appeal to Rs. 78,300 representing remittances of profits from this business outside British India were included by the Income-tax Officer in the taxable income in virtue of section 4(2) of the Act. The assessee claimed a deduction of Rs. 26,383 as interest on a sum which he had borrowed from the Punjab National Bank on the security of certain house property which he had mortgaged to the bank. The Income-tax Officer disallowed the deduction of this interest because the allowances under the head 'Property' were already in excess of the annual value and no further set off was permissible in view of the proviso to section 9 (1) of the Act. In appeal before the Assistant Commissioner it was contended on behalf of the assessee that the sum represented interest on capital borrowed for the purposes of business. The Assistant Commissioner thereupon caused a further enquiry to be made as a result of which it was ascertained that a sum of approximately Rs. 2,80,000 had been borrowed by the assessee from the Punjab National Bank and out of this sum Rs. 2,28,225 had been expended on the purchase of machinery for the Bhupindra Flour Mills and Rs. 33,313 on personal and private expenses.

The Assistant Commissioner in disallowing the claim made the following remark in his appellate order:—"The major portion of the capital borrowed was used for the purpose of purchasing machinery for the Flour Mills at Bhatinda which is situated outside British India. The interest at 9 per cent. on Rs. 2,28,225 is Rs. 20,540. The point for determination is whether the deductions enumerated in section 10(2) of the Income-tax Act can be allowed against the income of a *business situated outside British India*. Section 1(2) of the Income-tax Act shows that it does not apply to a business so situated. Section 4 applies to income received in British India and to profits and gains deemed under the provisions of the Act to accrue or arise, or to be received in British India. Section 6 shows the heads of income chargeable to income-tax, of which 'business' is one, and section 10 shows how the profits or gains of a business are to be computed. Now although section 4 specially provides for the taxation of income received in British India, or deemed to accrue or arise, or to be received in British India, sections 6 and 10 do not apply to businesses outside British India, because section 1(2) limits the extension of the Act to British India, save in the cases mentioned in that section. It cannot have been the intention of the Legislature to allow the deductions enumerated in section 10 in the case of business situated outside British India against receipts of income in British India, for the simple reason that if only a portion of income of a business situated outside British India were brought into British India, an assessee could evade the tax on it by claiming the deductions mentioned in section 10. The conclusion I have come to is that the interest claimed cannot be allowed in the circumstances, nor can the interest on the remainder

of the loan be allowed. The sum of Rs. 33,313 was utilized for private and personal expenses. The learned counsel for the assessee argues that the assessee spent more than the above sum out of his personal income on the business. We are not concerned with the destination of such income. The only point to be considered here is whether the capital borrowed on which interest is claimed was for the purpose of the business and the reply, as far as this item is concerned, is clearly in the negative."

Against this decision of the Assistant Commissioner the assessee filed an application under section 66(2) in which he asked that the following, among other points of law, should be referred to the High Court:—"Whether on a true construction of the Indian Income-tax Act interest on a loan raised for a business outside British India is not an allowable deduction and especially so when much larger profits of the business are taxed."

In dealing with this question the Commissioner, for the reasons given by him in his order, an extract of which is attached as Appendix 1,* agreed that when the profits of a business situated outside British India are being computed the interest on borrowed capital should be deducted in arriving at the net assessable figure. He however went on to make the following remarks:—"Although the point of law raised by the assessee has thus been conceded, it remains to be seen whether the assessment of the year in question must in consequence be modified. This would only be the case if all the profits of the Bhatinda Flour Mills made either during the accounting period, or within three years preceding the accounting period had been remitted to British India and had by virtue of section 4(2) of the Act been subjected to income-tax. The facts are however that the Bhatinda Flour Mills in the years in question made the following profits:..**

	Rs.
1922	.. 1,50,913
1923	.. 2,16,394
1924	.. 87,532
1925	.. 34,162
Total	.. 4,89,001

* Not printed.

**Strictly speaking the figures to be noted should have been as follows:—

	Rs.
1921	.. 49,614
1922	.. 1,30,913
1923	.. 2,10,057
1924	.. 47,040
Total	.. 4,37,624

The figures assessed as already noted are correct. No Profits were assessed in 1922-23.

As however the principle involved is not affected in any way, the mistake is immaterial.

Out of this total amount, which is the maximum which could possibly have come under assessment, the following amounts only were assessed in the corresponding assessment years:—

	Rs.
1924-25 ..	1,25,000
1925-26 ..	78,300
	—————
Total ..	2,33,270
	—————

It is clear from the above figures that a balance of Rs. 2,55,731 of un-assessed profits remains. The effect of my conceding the point of law raised by the assessee is that this balance is reduced by the amount of Rs. 20,540. The assessment of 1925-26 does not therefore require to be modified.”

The Commissioner thus decided that, although the question raised by the assessee could be answered in the affirmative, that answer had no effect on the assessment under consideration and for this reason he declined to make a reference to the High Court. Against this order the assessee presented a petition under section 66(3) to the High Court, and the Hon’ble Judges thereupon decided that assuming certain facts to be correct a question of law arises for decision as formulated below.

3. *Question of law to be referred.* It will be seen from the above statement that the facts assumed by the Hon’ble Judges and briefly stated in their order are correct. The question which the Hon’ble Judges have formulated is as follows:—“Should the amount of interest so paid be deducted from the profits received in British India, by virtue of clause (2) of section 10 of the Income-tax Act, though the whole of the profits made in the previous year as well as three preceding years may not have been brought into British India?”

4. *Opinion of the Commissioner.* In my opinion the answer to this question in the circumstances of this case should be given in the negative. Section 4(2) of the Income-tax Act (1922) provides that “profits and gains of a business accruing or arising without British India shall, if they are received or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose.” This sub-section thus renders liable to tax all remittances made to British India within the previous year out of business profits earned outside British India in the previous year, or in the three years preceding the previous year. Now, if we turn to section 10, we find that sub-section (1) provides that “the tax shall be payable by an assessee under the head ‘Business’ in respect of the profits or gains of any business carried on by him.” Sub-section (2) goes on “Such profits or gains shall be computed after making the following allowances”, and then follows a series of clauses defining these allowances, of which the relevant one for the present purpose is item (iii), which relates to interest paid in respect of capital borrowed for the purposes of the business. The Assistant Commissioner was apparently of the opinion that section 10 only applied to business income which actually accrued or arose in British India and not to such income which was ‘deemed’ under section 4(2) so to accrue or arise. I do not agree with this view. In my opinion sub-section (2) of section 10 may be taken to be an exhaustive explanation of what the Act intends when it uses the words “profits and gains of a business.” In other words, whether the business be situated inside British India or outside it, an Income-tax Officer in computing the profits should make the prescribed allowances. These

allowances are in any case based on the main principles of accountancy and must be borne in mind whenever commercial profits are being calculated. The question as it was originally framed by the assessee in his application under section 66(2) was therefore answered by me in the affirmative, and I agreed that the Bhatinda profits should be reduced by the amount of the interest paid on capital borrowed in British India for the Bhatinda business.

It now appears that what the assessee claims is that such interest should be set off against that part of the Bhatinda profits which was remitted to British India in the previous year and thus became chargeable to income-tax in the assessment under consideration. I submit that there is no warrant whatever for placing such a construction on the provisions of the Act. What the Income-tax Officer has to ascertain in such cases is, first, the actual amount of remittances into British India, and secondly, whether there were sufficient profits in the previous year to cover those remittances, or a sufficient balance of untaxed profits of the three preceding years which taken with the profits of the previous year would cover the remittances. This calculation has been made in the present case, and it is clear that there were ample profits to cover the remittances, even if those profits were reduced by the interest debited to the assessee's account by the Punjab National Bank. If the whole of the profits of the Bhatinda business had in fact been remitted to British India, then it would naturally follow that the allowance of the interest on borrowed capital would have reduced the amount liable to income-tax, because that amount could not exceed the net profits of the business. But since only a part of the profits were remitted, and the untaxed balance was more than sufficient to cover the interest which had accrued on the borrowed capital, the allowance of that interest cannot affect the assessment under consideration.

C. B. Petman and Madan Gopal, for the Assessee.

Jagan Nath Aggarwal, for the Crown.

JUDGMENT.

TEK CHAND, J.:—The assessee-petitioner is a resident of Lahore and has several sources of income in British India. He also owns a flour-mill, known as the Bhupindra Flour Mills, at Bhatinda in the Patiala State Territory. This Mill was burnt down some years ago but was renovated with money borrowed by the petitioner from the Punjab National Bank Ltd., Lahore. From 1921 onwards the petitioner has, from time to time, brought into British India a part, but *not* the whole, of his earnings from the Mill. The amount so brought within a particular year has been included in his assessable income for that year and to this the assessee did not—as he could not—raise any objection. He has, however, been claiming a deduction of the amount of interest paid by him during the accounting period to the Punjab National Bank on the loan above-mentioned. The question appears to have first arisen in connection with the petitioner's assessable income in the calendar year 1921 which was the basis of the assessment for 1922-23. On a reference by the Assistant Commissioner, the then Income-tax Commissioner (Mr. Darling) allowed the deduction holding that "expenses incurred outside British India may be set off against income taxable within British India; but it has to be remembered that under section 10(2) (iii) an interest charge is only liable as a deduction in respect of capital borrowed for the purpose of a business that is taxable. In this case, the income of the Bhupindra Mills is only taxable in so far as it is brought into British India within the statutory period. I think, therefore, that the interest allowed should not exceed the income taxed in British India, and it must, of course, have been paid in the "accounting year in question."

Similar deductions were admittedly allowed by the Income-tax authorities on the assessments for the years 1923-24 and 1924-25, which were made on the amount of profits of the Mill brought into British India in the calendar years 1922 and 1923 respectively. When the assessment for 1925-26 however, came to be made, the assessee claimed a similar deduction for interest paid to the Punjab National Bank in the calendar year 1924, but the Assistant Commissioner disallowed the claim on the ground that the allowances enumerated in section 10(2) of the Act could not be allowed against the income of a business situate outside British India. Against this order the petitioner moved the Income-tax Commissioner, who disagreed with the Assistant Commissioner in his view of the applicability of section 10(2), and held that there was no reason why the method of computing the profits and gains of a business should be different for a business not situated in British India and liable to tax under section 4(2). But while conceding this proposition in favour of the assessee, the Commissioner refused to allow the petitioner to deduct the amount of interest paid by him to the Bank in 1924 on the ground that under section 4(2), such a deduction could only be made if *all* the profits of the Bhupindra Flour Mills made *during the accounting period as well as within three years immediately preceding that period had been remitted to British India*. As it was admitted that the profits which had been made by the petitioner from the Mill in the calendar years 1921, 1922, 1923 and 1924 had not been received or brought into British India *in their entirety*, though during each of these years he had so brought more than the amount of interest paid to the Bank in that particular year, the learned Commissioner disallowed the deduction.

Thereupon the petitioner moved this Court under section 66(3) and Zafar Ali and Addison JJ. after stating the facts, passed an order requiring the Commissioner to state the case on the following question of law:—"Should the amount of interest so paid be deducted from the profits received in British India, by virtue of clause (2) of section 10 of the Income-tax Act, though the whole of the profits made (in the previous year as well as in the three preceding years) may not have been brought into British India?" We have examined the statement of the case submitted by the Commissioner and have also heard both counsel at length. After consideration I am of opinion that the law had been correctly laid down by Mr. Darling in his order dated the 11th of June 1924 and that the contrary view taken by his successor (Mr. Raisman) in the order under reference is not warranted by the provisions of the Indian Income-tax Act and cannot be sustained.

On behalf of the Income-tax Department, it is conceded that interest paid in British India for capital borrowed here for the purpose of a business conducted by the assessee in foreign territory, is a permissible allowance under section 10(2), if the profits or gains of such business are brought into British India. It is, however, contended that this deduction can be allowed only if *all* the profits earned by the assessee from such business in the accounting year and the three preceding years are brought in, and for this contention reliance is placed on clause (2) of section 4 of Act, which runs as follows:—"Profits and gains of a business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose."

Before the enactment of this clause it had been held that profits, which had arisen or accrued to a British Indian resident from a business outside British

India, but which had been subsequently transmitted to British India, were not his 'income' assessable under the Act, as a person could not receive his income twice over, and that the receipt in British India of such amount must be presumed to be that of capital *Sundar Das v. Collector of Gujrat*.⁽¹⁾ The Legislature considered this state of the law to be unsatisfactory and amended the Act by enacting that if profits of such business, earned in foreign territory, are brought into British India within three years from the end of the year in which they accrued or arose, the amount so brought shall be liable to assessment. The practical effect of this provision is to lay down that the profits of a foreign business brought into British India shall be deemed to be his *assessable income* if they are brought within three years of the end of the year in which they are earned, but they will be treated as his *capital* (and therefore immune of assessment) if they are so brought after the expiry of that period. By fixing this arbitrary limit of three years the Legislature has, on the one hand, provided against the evasion of the law by the assessee bringing in his foreign income at intervals and urging that it was not received in British India in the year in which it was earned and had thus become his capital and on the other, it has recognized the principle that if foreign profits are not brought into British India within a reasonable period (i.e., three years from the end of the year in which they were earned) they shall be treated as having become his savings or capital, and not liable to assessment, if brought after the expiry of that period. The clause does not, however, lay down expressly, or by necessary implication, that any allowances which might be permissible, under section 10(2), in determining the amount of these profits or gains, should be given credit for only if *all* the profits made by foreign business in the accounting period and the three years immediately preceding thereto are transmitted to British India.

It must be remembered that by the law of India, a present resident in British India cannot be taxed in respect of his earnings from a trade or business carried on abroad, irrespective of whether such earnings have or have not been brought into British India; but it is only that portion of such earnings which is *actually brought* into British India during the period mentioned above, which is to be deemed to be his "profits and gains", and as such liable to be taxed. If in determining the "profits" of such business any allowances are permissible under section 10(2), I cannot see why the assessee should lose his right to claim them, merely because he has not brought into British India his foreign profits for the accounting period, or for the three preceding years in *their entirety*. After carefully considering the provisions of the Act, I have no doubt in my mind that the permissible deductions should be allowed subject, of course, to the limitation pointed out by Mr. Darling in his order referred to above, that the amount so set off does not exceed the amount brought into British India and taxed in the accounting year.

It is admitted by both parties that during the accounting period in question (which is the calendar year 1924) the Mills made a total profit of Rs. 47,040 only, but during this period the assessee remitted to British India from Bhatinda Rs. 78,300 comprising the entire earnings of that year as well as Rs. 31,260 out of the savings of the previous years, and that this sum of Rs. 78,300 has been included in his assessable income. As against this he claimed a deduction of Rs. 20,450 only, being the amount paid by him to the Punjab National Bank during the same period as interest on the loan which had been raised for the purposes of the Mill.

The amount of foreign profits brought into British India in the accounting period is thus far in excess of the amount of interest paid during the period,

(1) 1 I. T. C. 189.

and, therefore the latter amount is a permissible allowance under section 10(2) and the assessee is entitled to deduct it from his assessable income.

I would, therefore, answer the question in favour of the assessee and allow him his costs in this Court.

AGA HAIDER, J.:—I agree.

(371) IN THE HIGH COURT OF JUDICATURE OF MADRAS.

Before Sir Owen Compton Beasley, Kt., Chief Justice, Mr. Justice Anantakrishna Ayyar and Mr. Justice Curgenvven.

(1st May, 1930).

S. P. S. Ramaswami Chettiar and others .. Assessee.*

v.

The Commissioner of Income-tax, Madras .. Referring Officer.

Indian Income-tax Act (XI of 1922), Sec. 10—Money-lending business—Loss by theft of money used in business—If allowable in assessment of profits.

Per the Chief Justice and Curgenvven, J. (Anantakrishna Ayyar, J. dissentiente):—

Where the assessee carrying on money-lending business had the strong room in his business premises broken into by thieves—his former cook being one of them—who stole cash and currency notes used in the business, the loss so incurred is not allowable in the computation of his assessable profits, such loss not being incidental to the business.

Case (O.P. No. 275 of 1928) stated under Sec. 66(3) of the Indian Income-tax Act, (XI of 1922) by the Commissioner of Income-tax, Madras, in compliance with the order of the High Court, dated 10th October, 1929.

CASE.

In accordance with the High Court's order I have the honour to refer the following case for the decision of the Hon'ble the Judges of the High Court under section 66(3).

2. The facts are as follows: The petitioners are a registered firm carrying on banking business at Karaikudi, Kayan, Moulmeingyun and Einme in British India and at Kualalampur in Federated Malay States with their headquarters at Karaikudi in the Ramnad District within the jurisdiction of the Income-tax Officer, Karaikudi, I Circle.

3. On the night of 21st October 1926, certain persons broke into the strong-room of a house at Moulmeingyun occupied by the petitioners and by two other firms, and stole cash and currency notes of the value of Rs. 9,335, besides certain jewels not now in question. On 5th August, 1927, four persons were convicted of the said offence by the Special Power Magistrate, Myaungmya. One of these persons had been employed as a cook at the above-mentioned premises, but was not so employed at the time of the offence. This person was convicted in addition under section 328 Indian Penal Code of administering

* (1930) I. L. R. 53 Mad. 904; 53 M. L. J. 403; 33 L. W. 237; A. I. R. (1930) Mad. 803.

drugs to the inmates of the house to facilitate the commission of the theft. Adjoining the house were a kitchen and cattle-shed and it may be taken that the house was used partly for the business of the firm and partly as a residence.

4. The petitioners claimed that this sum of Rs. 9,335 should be allowed as expenditure in computing the profits of their Moulmeingyun branch. The claim was disallowed on the ground that the loss was of a capital nature. On application being made to me to state a case to the High Court, it appeared to me that the sum in question had not been lost or expended in the course of the petitioners' business, and that in this state of the facts no question of law could arise.

5. In the above order the High Court has directed me to refer the following question:—"Whether the loss incurred by theft of money used in the money-lending business and in the business premises should be allowed for in computing the income-tax".

6. The deductions to be allowed in computing the profits of a business are described in section 10, sub-section (2) of the Indian Income-tax Act, XI of 1922. In my opinion the deduction now claimed is not covered by any of the provisions of that sub-section. Clauses (i) to (viii) refer to rent, cost of repairs, interest on capital, insurance premium, allowance for depreciation, land revenue and local taxes. The present claim does not come under any of these descriptions. Clause (ix) refers to "any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains". The sum claimed here is not money expended or laid out. It is not expenditure, but an accidental loss. I do not consider that a loss is a kind of expenditure, but even if I am wrong in this it cannot be said that this loss was "incurred solely for the purpose" of earning the profits and gains of the business.

7. In my opinion the loss was not one incurred in the business at all. The petitioners quote the analogy of money lent out and found to be irrecoverable. But the loss of money lent out is in my opinion a result of business transactions, whereas the loss now claimed is due to an occurrence which was not part of the business at all and had nothing to do with it. It is also claimed that this loss should be allowed because a loss due to embezzlement by an employee is allowable. The decision in *Jagarnath Theroni v. Commissioner of Income-tax, Behar and Orissa* (1) is quoted in this connection. The ground of that decision is that loss springs directly from the necessity of deputing certain duties to an employee; in other words, is one incurred in the course of the business. It seems to follow from this that a loss due to theft committed by persons unconnected with the business is not allowable.

V. Rajagopala Ayyar, for the Assessee.

M. Patanjali Sastri, for the Crown.

JUDGMENT.

THE CHIEF JUSTICE:—The facts in this case have been sufficiently set out in the answers to the question referred to us of my learned brothers Anantakrishna Ayyar and Curgenvin JJ. which I have had the advantage of seeing and I therefore do not propose to state them. The question seems to me to resolve itself into one as to whether the loss sustained by the assessee in this case was one which can be described as incidental to his business. If it

was, then he is entitled to have his profits upon which he is liable to pay income-tax reduced by the amount of that loss. It was argued for the assessee (1) that the robbery of the assessee's money was one which was incidental to his business of a money-lender and (2) that the money stolen was his 'stock-in-trade' because it was money which, had it not been stolen, was available to him for the purpose of lending to borrowers and making a profit thereby. There is no evidence in this case that this sum was 'stock-in-trade' at all and the money would seem to me to be capital plus the profits collected by the assessee. If this money was capital, then the assessee would not be entitled to a deduction on account of its loss.

So far as the money stolen was the profits of the assessee, unless it can be shown that its loss was incidental to the business he carried on he cannot claim a deduction in respect of it. If any one is paid a sum due to him as profits and he puts that in his pocket and on his way home is robbed of it, it would be, I think, difficult to contend that such a loss was incidental to his business. Still more so when he has reached his home and put those profits in a strong room or some other place regarded by him to be a place of safety. I can well understand that in cases where the collection of profits or payment of debts due is entrusted to a gumastah or servant for collection and that person runs away with the money or otherwise improperly deals with it, the assessee should be allowed a deduction because such a loss as that would be incidental to his business. He has to employ servants for the purpose of collecting sums of money due to him and there is the risk that such servant may prove to be dishonest and instead of paying the profits over to him convert them to his own use. But I cannot distinguish the present case from the case of any professional man or trader who, having collected his profits, is subsequently robbed of them by a stranger to his business. In this case none of the thieves were the then servants of the assessee although one of them had formerly been his cook. This is no doubt a very hard case and, whilst I have every sympathy with the assessee, I am unable to answer the question except in the negative. The question referred to us is rather too general but upon the facts of this case which, in my opinion, are not at all adequately set out, that must be my answer.

The result is that the answer of this Full Bench is in the negative and the assessee is directed to pay the costs of the Income-tax Commissioner which we fix at Rs. 250.

ANANTHAKRISHNA AIYAR J:—I have the misfortune in this case to differ from the opinion of my Lord the learned Chief Justice, and of my learned brother Curgenvin J.

The question referred for our decision under section 66 of the Indian Income-tax Act is "Whether the loss incurred by theft of money used in the money-lending business, and in the business premises should be allowed for in computing the income-tax."

The question raised is one of very great importance, and the case is one of first impression, no case directly deciding the point having been brought to our attention.

One should have liked that more facts were available; the facts, as they appear in the records before us, are the following:—The petitioners are a registered firm of Nattukottai Chetties carrying on money-lending business at Karaikudi and other places in British India, and at Kuala Lumpur in Federated Malay States, the headquarters being at Karaikudi in the Ramnad District. On the night of the 21st October, 1926, certain persons broke into the strong room of

the house at Moulmeingyum (Burmah) occupied by the petitioners and by two other firms, and stole cash and currency notes of the value of Rs. 9,335 besides certain jewels which had been pledged with the firm, as security, by certain customers. On 5th August, 1927, four persons were convicted of the said offence by the Magistrate. One of these persons had been employed as a cook at the abovementioned premises. Though he was not so employed at the time of the offence, he was convicted, in addition, under section 328 Indian Penal Code, of administering drugs to the inmates of the house to facilitate the commission of the theft. The Commissioner of Income-tax stated that he had since the decision of the Income-tax Officer ascertained that the loss of the cash and the jewels was genuine. He however was of opinion that there was no provision of law under which the assessee would be entitled to deduction claimed in respect of the cash and currency notes, that the loss could neither be said to be a business loss, nor expenditure incurred for earning profits; and that the loss in question is loss of capital. The decision in *Jagarnath Therani v. Commissioner of Income-tax, Behar and Orissa*(1) was distinguished on the ground that the loss in the present case could not be said to have been incurred in the business at all, and that such a loss could not be said to have been incurred solely for the purpose of earning the profits and gains of the business. He therefore held that the loss due to theft committed by persons unconnected with the business is not allowable as a deduction.

The learned Counsel who appeared in support of the assessment argued that the allowance now claimed could not be brought under any of the clauses of section 10 of the Act, which, he argued, exhausted the headings under which allowances could be claimed by assessee. I am unable to accede to that contention. Section 10 no doubt directs that the allowances mentioned in the section should be made in favour of the assessee; but in my view it does not necessarily follow that the assessee is not entitled to the allowances now in question simply because it is not specifically mentioned in section 10. Under clause 1 of section 10 tax is payable only in respect of the profits or gains of any business carried on by the assessee. The Court has to find out what the profits or gains of the business amounted to. In the absence of any specific provisions in the Act, the profits or gains of a business have to be ascertained by the ordinary commercial methods. If the argument advanced on behalf of the Crown be accepted, it would follow that no allowance could be claimed, for instance, for bad debts actually written off during the year, since there is no specific provision in section 10 for allowing such deduction. But it could not be, and in fact was not, contended that allowance should not be made for such bad debts. The practice of making allowance for such bad debts has become firmly established. As the Court has to find out the amount of profits or gains of the business during the period, the question arises whether the loss by theft in question should be deducted when the profits are ascertained.

As pointed out in Konstam's book, "The net profits of the trade or business should be computed by reasonable business methods, subject to any specific directions contained in the Income-tax Act". Lord Herschell observed, in *Russell v. Town and County Bank*(2) as follows:—"The profit of a trade or business is the surplus by which the receipts from trade or business exceed the expenditure necessary for the purpose of earning those receipts***** Unless and until you have ascertained that there is such a balance, nothing exists to which the name of profits can properly be applied." Similar observations were made by Lord Parker in *Usher's Wiltshire Brewery, Ltd. v. Bruce*(3), "Where a deduction is proper and necessary to be made in order to ascertain the balance of profits and gains, it ought to be allowed***** provided there is no prohibition against such an allowance."

(1) 2 I. T. C. 4.

(2) 2 Tax Cas. 321; 13 App. Cas. 418.

(3) 6 Tax Cas. 399; (1915) A. C. 483.

It was argued for the assessee that the allowance claimed would come under section 10(2) (ix), "Any expenditure not being in the nature of capital expenditure incurred solely for the purpose of earning such profits or gains." It was also argued that in the case of money lending business of Nattukkottai Chetties the loss in question must be taken to be loss of stock in trade. On the other side, it was argued for the Crown that the loss in question could not be said to be an expenditure incurred, much less, solely, for the purpose of earning such profits or gains, and that in any event it should be taken to be expenditure in the nature of 'capital' expenditure. It was also argued that the moneys in question could not be said to be 'stock-in-trade' in the ordinary sense of the expression. Having regard to the way in which such people carry on their money-lending business, it would seem to be essential for the successful carrying on of their business to have cash with them even after 'the usual banking hours.' They carry on their business operations, as is well known, even after the offices of the European Banks are closed for business for the day. Keeping monies with them for purposes of their trade after such office hours, could not, therefore, in my view, be said to be anything else than keeping monies in the usual course of their business. The profits made by them by doing business after the usual office banking hours are surely liable to income-tax. The finding, as I understand it, is that in the usual course of business the remaining cash, etc., on hand and the jewels received on pledge from the customers were kept in 'the strong room' of the business premises, and that thieves broke into the strong room and stole the cash and currency notes and the jewels. The fact of theft having been found, I think that the loss in question should be taken to be a loss connected with or arising out of the money-lending trade or business of the assessee. With reference to the jewels thus lost, the Income-tax authorities have, and, in my opinion, rightly, made allowance; but I think that allowance should be made also for the cash and currency notes amounting to Rs. 9,335 thus lost.

I am unable to agree with the contention of the Crown that the loss in question, should, if at all, be taken to be loss of 'capital'. It is true, as pointed out on behalf of the assessee, that the profits of the Moulmeingyum business for the period in question was computed by the Income-tax authorities to be over Rs. 20,000. But that circumstance by itself is no ground for holding that the item in question should be taken as loss of profits, and not loss of capital. Whether a particular item is really capital expenditure or not has to be decided having regard to various considerations. Of course it is well established that when once profits have been earned during the period, it does not matter how the same is dealt with subsequently.

I am inclined to the view that in the case before us, the cash and currency notes, etc., lost should be taken to be 'stock in trade' of the assessee's business. What should be considered as stock in trade of a business should be decided after having regard to the nature of the particular business, its requirements, and other circumstances essentially connected with the successful carrying out of the particular business.

In *The Punjab National Bank, Ltd., v. Commissioner of Income-tax, Punjab*(1) the question was raised whether allowance should be made for depreciation in the case of certain Government securities held by a firm. The answer would depend on the question whether those securities were held by the firm (Bank) with the object of dealing with them from day to day in the ordinary course of its business including that of buying and selling Government

securities in the usual course, or whether such Government securities were purchased by the firm (Bank) with the object of constituting the same as a reserve in lieu of cash. In the case of the former allowance should be made for depreciation (the reason being that the Government securities should, in such a case, be treated as 'stock in trade' of the Bank); but not in the case of the latter.

In the case of money-lending business such as the one before us, I think that the reasonable view to take as regards stock in trade is the one indicated by me before.

The decision in *Jagernath Therani v. Commissioner of Income-tax, Bihar and Orissa*(1) so far as it goes also supports this view. There, some money was entrusted to a Gumastha of a firm in the usual course of business with instructions to pay the same to a creditor of the firm. The Gumastha embezzled the monies. He was criminally prosecuted, but was acquitted, his defence being that he was robbed of the money. The case however, was comparatively a plainer case than the one before us, and the Court, if one may say so with respect, very properly held that the loss was connected with and arose out of the business, and was not *prime facie* a loss in the nature of capital expenditure.

On behalf of the assessee, the decision of Rowlatt, J., in *Curtis v. J. and G. Oldfield, Ltd.*(2), was referred to before us. At page 330 the learned Judge observed as follows: "I quite think, with Mr. Latter, that if you have a business, in the course of which you have to employ subordinates, and owing to the negligence or the dishonesty of the subordinates, some of the receipts of the business do not find their way into the till, or some of the bills are not collected at all, or something of that sort, that may be an expense connected with and arising out of the trade in the most complete sense of the word." Stress was laid on the words 'something of that sort' occurring in that judgment. But the words are too wide, and one cannot be certain that the learned Judge had a case like the present in his view. Too much importance should not, I think, be attached to the above observation in the circumstances.

It was argued on behalf of the Crown that theft should not be taken to be anything connected with or arising out of the assessee's money-lending business. In my view that is stating the position rather too broadly. In the case of Railway administrations and other common carriers, the practice seems to be to make allowance for losses sustained by them in compensating passengers for accidents in travelling over the railway, etc. That the practice is to make such allowance in favour of common carriers is taken for granted in the judgment of Loreburn, L. C., in *Strong and Company, Ltd., v. Woodfield*(3). At page 219 the Lord Chancellor observed as follows: "In my opinion, however, it does not follow that if a loss is in any sense connected with the trade, it must always be allowed as a deduction; for it may be only remotely connected with the trade, or it may be connected with something else quite as much as or even more than with the trade. I think only such losses can be deducted as are connected with, in the sense that they are really incidental to, the trade itself. They cannot be deducted if they are mainly incidental to some other vocation or fall on the trader in some character other than that of trader. The nature of the trade is to be considered. To give an illustration, losses sustained by a railway company in compensating passengers for accidents in travelling might be deducted."

(1) 2 I. T. C. 4.

(3) 5 Tax Cas 215.

(2) 9 Tax Cas 819.

If losses sustained by a railway company in compensating passengers for accidents in travelling over its line could be deducted, it would seem to follow that losses similarly sustained by a railway company in compensating owners and consignees of goods entrusted to them for carriage, but which were lost during transit by theft, could also be deducted in proper cases. That would seem to resemble the present case, and the observations by the Lord Chancellor, I think *prima facie*, support the contention of the assessee before us.

No doubt the further observations made by the Lord Chancellor should also be kept in view. It was remarked later on, at page 219 "Many cases might be put near the line, and no degree of ingenuity can frame a formula so precise and comprehensive as to solve at sight all the cases that may arise."

The loss must be something in the nature of a commercial loss. Whether a particular loss is of that nature or not would have to be decided with reference to all the circumstances of a case. In *Royal Insurance Co. v. Watson*(1), Lord Shand expressed the opinion that damages awarded to an employee for wrongful dismissal would be allowable as a deduction. Damages for libel against a newspaper proprietor would appear to be loss in the ordinary course of business of proprietors of newspapers. See Pratt and Redman's Income-tax Law, 10th Edition page 112.

To the argument urged on behalf of the Crown that it is no part of the assessee's business to deal with thefts, the following observations of Lord Buckmaster in *Green v. Glikstein and Son, Ltd.*(2), may be referred to. There the question was whether the amount received by a firm of timber merchants from Fire Insurance, Co., in respect of stock of timber destroyed by fire could be assessed to income-tax. At page 384, [(1929 A.C.)] Lord Buckmaster observed as follows: "If this results in a gain as it has done it appears to me to be an ordinary gain—a gain which has taken place in the course of their trade—none the less because, as Mr. Macmillan put it, and as I think Sir John Simon before him appears to have put it, it is no part of a timber merchant's business to trade in fires."

If in the present case the stock in trade of the assessee before us including balance on hand each day and the jewels, etc., received on pledge from customers, had been insured at a particular figure against fire or theft, and the amount was accordingly received from the insurers on the occurrence of fire or theft, then the amount so received would, according to the decision in *Green v. Glikstein & Sons, Ltd.*(2) be *prima facie* taxable. The premia paid in respect of such insurance is allowed to the assessee [(See section 10 (2) (iv)], and in return, the amount received by the assessee from the insurers would seem liable to be assessed to income-tax. If no insurance had been effected by the assessee, no premium is paid and no allowance is made on account of premium; and in case of loss, the assessee receives no amount from insurers, and therefore no such amount could be included in the assessment. The reasoning would seem to lead to the conclusion that the loss even if un-insured should be deducted, as I have come to the conclusion that the loss is connected with the business and is really incidental to the trade itself having regard to the nature of the trade or business of the assessee.

Turning to English text-books on Income-tax law, I find the following statements in Sanders' Income-tax—3rd edition. At page 310, it is stated that "a deduction is allowed in respect of employees' theft". At page 196, it is stated, that "loss from embezzlement is deductible". Similarly at page 163,

(1) 3 Tax Cas. 500; (1897) A. C. 1.

(2) 14 Tax Cas 365.

“deduction is allowed in practice for the loss arising from defalcations of employees”. At page 203, there are two passages which are rather important, “a deduction is permitted in practice for fire insurance premiums”; also, “loss of stock through fire is deductible in so far as it is not recovered by insurance, but loss of building does not form an admissible deduction.” I also note that, “loss by flood or tempest” is allowed in case of assessments under Sch. A. The above statements, so far as they go, would seem to lend support to the assessee’s contention in the present case.

Each case has to be decided with reference to the facts and circumstances relating thereto and having regard to the nature and methods of trade or business in question. Having regard to the circumstances of the present case, and the findings of fact arrived at by the Income-tax Commissioner, I think that the assessee is entitled to the deduction of Rs. 9,335 claimed by them, and I would answer the question in the affirmative.

CURGENVEN J:—The question which the Commissioner refers is: “Whether the loss incurred by theft of money used in the money-lending business and in the business premises should be allowed for in computing the income-tax.”

The Commissioner rightly observes that a loss of this character is not included within any of the deductions permissible under section 10(2) of the Act. But that does not conclude the matter, because section 10 provides for the taxation of the profits of a business, and we have therefore to consider whether, in computing profits, the amount of such a loss may be deducted from them. It is settled for instance, that a bad debt incurred by a money-lender may be so deducted, on the ground that it is a loss incidental to his business, so that it is fair, in assessing his net profits, to take account of losses as well as gains. Such a loss, it appears to me, must satisfy two conditions, (1) it must be a loss of part of the stock in trade of the business, and (2) it must be a loss of such a kind as is incidental to the business.

As regards (1), the question describes the money lost as ‘money used in the money-lending business,’ and taking this to mean money actually in use in the carrying on of the business, I feel no difficulty in holding that it was part of the money-lender’s stock in trade. It may have included profits earned in previous transactions, but if those profits were themselves to be applied to the business, and were kept in hand for that purpose, they would not, I think, be any the less part of the stock in trade.

Requirement No. (2) presents greater difficulties, because I think it is clear that not all kinds of losses of stock in trade can be said to be incidental to the business. A loss, to be incidental, must be such as in the ordinary course, and having due regard to the peculiar risks attendant upon the conduct of the business, is likely from time to time to occur. Cases of embezzlement by subordinates, such as formed the subject of *Jagarnath Therani v. Commissioner of Income-tax, Bihar and Orissa*(1) would be losses of this nature, because the employment of clerks and servants is unavoidable, and the employer is likely sooner or later to be the victim of their dishonesty or negligence. That such a loss might be classed as a form of expense arising out of trade was recognised in *Curtis v. J. and G. Oldfield, Ltd.*(2), although in the particular circumstances

(1) 2 I. T. C. 4.

(2) 9 Tax. Cas. 319.

of that case, as I read it, the money lost no longer formed part of the stock in trade.

The test whether the loss was, in the language of the English rule, "connected with or arising out of trade", was applied in two other English cases, *Strong & Co., Ltd., v. Woodfield*(1) and *Inland Revenue Commissioner v. Warnes & Co.*(2). The former related to damages claimed from an inn-keeper in respect of injuries caused to a customer by the falling of a chimney; the latter to a penalty incurred by a trading firm for negligently failing to observe certain conditions imposed during war-time on the export of goods to neutral countries. The loss was held, in the language of the English rule, to be a loss "not connected with or arising out of trade". These cases do not help us further than to show what manner of test should be applied.

Now in the present case it may be conceded that a money-lender's business requires that he should keep a considerable sum in cash on his premises. Even if a Bank is accessible to him, it would unduly restrict his activities to transact his affairs only within banking hours. The practice is certainly otherwise, and it is only fair to have regard to custom in deciding what the exigencies of a business require. That means that cash must be kept in a safe or strong room. The receptacle in the present case is described as a strong room and the question resolves itself into whether theft from a strong room may form the foundation of a claim to remission of tax. I exclude cases of theft by a clerk or servant employed in the business and having access to the strong room, because that is not in question here and special considerations might apply. In general, I am not prepared to say that theft by some external operator, with or without the complicity of domestic servants, ought to be recognised as the basis of a claim. To recognise it we must, I think, find, not only, that the cash had to be kept on the premises, but that its loss by theft was a circumstance which was so far probable as to be an occurrence incidental to, if not inseparable from, the manner in which it had to be kept. In my experience, the abstraction of money by theft from properly constructed safes or strong rooms is not within the competence of the ordinary thief or house-breaker, and we have not yet in this country to reckon with gangs of safe-breakers such as may be found elsewhere. Perhaps the circumstance that no decision upon a case of this nature is to be found suggests the infrequency of such claims. The only test to apply, in order to see whether a loss of this kind is one incidental to the business, is, I think, the comparative likelihood of its occurrence, the requirements of the business being what they are. For example, injury to life and limb, and probably theft too, must occur sooner or later in the running of a railway. Bad debts and embezzlement have already been adverted to. Very likely the theft of stock in trade which have to be kept exposed to the public would fall into the same category. But I doubt whether cash kept in a safe should, if it should happen to be stolen, be allowed for.

We have not been furnished with any adequate narration of the facts of the present case, so that the question has had to be answered as indeed it is put, in general terms. So considering it, I agree with my Lord in returning a reply in the negative.

SATYENDRA MOHAN v. COMM. OF INCOME-TAX, BENGAL. 447
(372) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin Kt., Chief Justice,
Justice Sir C. C. Ghose, Kt., and Mr. Justice Buckland.*

(5th May, 1930).

Satyendra Mohen Roy Choudhury and others .. Assessee.*

v.

The Commissioner of Income-tax, Bengal .. Referring Officer.

Indian Income-tax Act (XI of 1922) Secs. 23 (4) and 34—Estimate Assessment—Income escaping assessment under specified heads—Notice to enhance assessment—Alleged over-assessment of other income—Assessee, if entitled to re-open entire assessment.

Where an assessment under Sec. 23 (4) of the Income-tax Act is re-opened under Sec. 34 by reason of income from certain specified heads having been assessed at too low a figure and proceedings are taken to increase the assessment, it is not open to the assessee to show that at the original assessment his income under other heads not in any way intermixed with the income from the specified heads have been assessed at too high a figure unwarranted by law. It is always open to him to show in any way he can, e.g., assessment under a different head or as from a different source, that the income alleged to have escaped assessment has not in truth and in fact escaped assessment and for this purpose income, profits or gains have not necessarily escaped assessment because they have not been assessed under the right head.

Reference under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal for the opinion of the High Court.

CASE.

I have the honour to state the following case for the decision of the Hon'ble High Court under section 66(2) of the Act.

2. The following are the facts of the case:—Messrs Satyendra Mohon, Hemendra Mohon and Nalini Mohon Roy Choudhury, the three brothers forming a Hindu undivided family, hereinafter called the assessee, have got assessable and non-assessable sources of income. The assessable sources with which we are concerned consist of money lending business, house property and other sources, viz, rents from non-agricultural lands in zemindary. Their accounting year is the Bengali year which usually ends in April. In the present reference we are concerned with the assessment under section 34 for 1926-27 based on the income of the accounting year 1332 B. S.

The assessee were originally assessed for the year 1926-27 on an estimated income of Rs. 11,155 from business, Rs. 1,795 from property and Rs. 5,000 from other sources under section 23(4) in the absence of return and accounts. In the course of examination of accounts requisitioned by the Income-tax Officer in connection with the assessment for 1927-28 the Income-tax Officer discovered that the income of 1925-26 (1332 B. S.) under head "business" and "property" had partially escaped assessment.

* (1930) 34 C. W. N. 816; A. I. R. (1930) Cal. 627.

Accordingly on the 14th September, 1927, he issued a notice under section 22 (2) read with section 34 informing the assesseees that their income of the year 1332 B. S. under the heads "business" and "property" had partially escaped assessment and calling for a revised return of income of that year. The assesseees duly filed a return of income from all sources in respect of the year in question. In addition they claimed rebate of Rs. 7,373 on account of life insurance premia paid. This claim was not made at the time of the original assessment. Subsequently in compliance with a notice under section 23 (2) they produced accounts and claimed that the income under the head "other sources" had been overassessed at the time of the original assessment. The Income-tax Officer did not consider either of these points, as he thought that in an assessment under section 34 he was only concerned with the income under the heads "business" and "property," which had escaped assessment, and that it was not open to him to revise the original assessment generally. On appeal the Assistant Commissioner of Income-tax took the same view except that he allowed the rebate on life insurance premia. The assesseees have now petitioned me to revise the assessment under section 33, or in the alternative to refer the following question of law to the Hon'ble High Court:—"When an assessment made under section 23 (4) of the Act is reopened under section 34 by reason of the income from certain specified heads having been assessed at too low a figure, and proceedings are taken for the purpose of increasing the assessment, is it open to the assessee to show that his income under other heads had been assessed at the original assessment at too high a figure and that such assessment was unwarranted by law."

I have declined to interfere in revision and accordingly refer the question with my opinion which is as follows: Section 34 provides for the assessment of income, profits, or gains, which has escaped assessment in any year, or which has been assessed at too low a rate, but gives no general powers of revision to the Income-tax Officer. That is to say, if the Income-tax Officer discovers that an assessee had income, profits, or gains from any source which escaped assessment in any year he may proceed to assess such income, profits, or gains, and if the rate applicable to the total income of the assessee for that year is affected, may proceed to reassess such total income. He cannot, however, reopen the assessment of the income, profits or gains of an assessee from any source in respect of which he has no reason to believe that this assessee has been underassessed. It appears to be the intention of the Act that general powers of revision should only be exercised by the Commissioner acting under section 33. The power granted to the Income-tax Officer under section 27 is not a power of revision but a power to start assessment proceedings afresh under particular circumstances, while his powers under sections 34 and 35 are strictly limited by the terms of the sections themselves.

A. C. Gupta and B. C. Das Gupta, for the Assesseees.

The Advocate-General and R. B. Pal, for the Crown.

JUDGMENT.

RANKIN, C. J.:—The assesseees are a Hindu undivided family and for the year 1926-27 an assessment to income-tax was made upon them under section 23, clause (4), upon the footing that they had made default in rendering a return of income and submitting accounts. The Income-tax Officer making the assessment to the best of his judgment, assessed upon a total income of Rs. 17,950 under the following heads: Money lending business, Rs. 11,155, property, Rs. 1,795, other sources, Rs. 5,000 making in all Rs. 17,950. In connection with the assessment for the next year, namely, 1927-28 the assesseees produced certain

accounts from which the Income-tax Officer was of opinion that in the previous year income under the heads business and property had partially escaped assessment. Accordingly, under section 34 of the Act he issued a notice stating that he had reason to believe that their income from money-lending and house property chargeable to income-tax in the year ending 31st March, 1927, had partially escaped assessment and that he proposed to assess the income that had escaped assessment and requiring the assessee to deliver a return of their income from all sources chargeable to income-tax during the said year. In compliance with this demand, the assessee filed a return showing that their income chargeable in the said year was (a) from money-lending business, Rs. 28,287-11-0, (b) from house property, Rs. 1,365, (c) from other sources Rs. 281, making a total of Rs. 29,933-11-0. Upon the basis of this return, and after an examination of the accounts, the Income-tax Officer re-assessed the petitioners as follows:—Business, Rs. 28,787; property, Rs. 3,071; other sources, Rs. 5,000 as originally assessed, making a total of Rs. 36,858. It will be seen, therefore, that as regards money-lending business the Income-tax Officer has raised the assessment from Rs. 11,155 to Rs. 28,787; and as regards property from Rs. 1,795 to Rs. 3,071.

Upon the present reference the decision of the Income-tax Officer is not challenged as regards these items. What is contended by the assessee is that the Income-tax Officer was wrong in thinking himself entitled to repeat the original assessment under the heading "other sources" at the figure 5,000. The contention which they seek to raise is that the Income-tax Officer, acting originally to the best of his judgment under section 23, clause (4), assessed them under the head "other sources" at a figure which was much too high; that he had wrongly assumed that a certain portion of their collections from their zemindaries was chargeable to income-tax, whereas in fact a much smaller portion was so chargeable, a great bulk of this revenue being agricultural.

The income-tax authorities have held that this contention cannot be raised in the present proceedings under section 34; that these proceedings were for the purpose of assessing income from money-lending business and house property which had partially escaped assessment; that the question whether the assessee's collections from their zemindaries are or are not, to the extent claimed, agricultural income, has nothing to do with the question whether the original assessment was too low in respect of their money-lending business or their property—i.e., buildings or lands appurtenant thereto (Cf. section 9).

The question which has been referred to us is stated as follows:—"When an assessment made under section 23 (4) of the Act is re-opened under section 34 by reason of the income from certain specified heads having been assessed at too low a figure and proceedings are taken for the purpose of increasing the assessment, is it open to the assessee to show that his income under other heads had been assessed at the original assessment at too high a figure and that such assessment was unwarranted by law?"

The Commissioner of Income-tax is of opinion that section 34 provides for the assessment to income-tax of profits or gains which have escaped assessment in any year, or which have been assessed at too low a rate; that it gives no general powers of revision to the Income-tax Officer and that the Income-tax Officer cannot re-open the assessment of the income, profits or gains of an assessee from any source in respect of which he has no reason to believe that the assessee has been under-assessed. In his view, it appears to be the intention of the Act that general powers of revision should only be exercised by the Commissioner acting under section 33 and that the powers of the Income-tax Officer under sections 34 and 35 are strictly limited by the terms of the sections themselves.

Mr. Gupta, for the assessee, has contended that section 34 says nothing about heads of income or sources of income. Accordingly, he contends that one has to look at the total assessment before one can decide whether any income has escaped assessment. While not disputing that steps taken under section 34 cannot give rise to a right in the assessee to make a claim for a refund and that the Income-tax authorities may at any time abandon the proceedings under this section, he contends that such proceedings entitle the assessee to show that while income under one head may have escaped assessment, income under another head had been over-assessed—in other words, that the whole assessment may be re-opened at the option of the assessee who may show what the real truth as to his total income is.

This controversy must be determined, if possible, upon the words of the section which are as follows:—“If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section: Provided that the tax shall be charged at the rate at which it would have been charged had the income, profits or gains not escaped assessment or full assessment, as the case may be.” The section begins by contemplating a case in which income, profits or gains has escaped assessment and it says that the Income-tax Officer may serve a notice upon the person liable to pay tax on such income. The notice may contain all or any of the requirements which may be included in a notice under section 22 (2). The ultimate step is that the Income-tax Officer may proceed to assess such income. The words which have reference to a case in which income has been assessed at too low a rate may, for the present purposes, be disregarded as they refer to a separate type of case. Broadly speaking, as the section is expressed, it deals with income which has escaped assessment and it provides how the Income-tax Officer may proceed to assess it.

In the present case the assessee's income from their business is found to have been Rs. 28,787 of which all but Rs. 11,155 has escaped assessment; and their income from property is found to have been Rs. 3,071 of which the excess over Rs. 1,795 has escaped assessment. I do not think that it can be said in such a case as this that the sums which represent the difference, i.e., Rs. 17,632 and Rs. 1,276 are not income which has escaped assessment because the assessee's have been charged too much in respect of the zemindari collections. If the question of the zemindari collections was in any way inter-mixed with the question of the profits in the money-lending business, or the question of the assessee's property within the meaning of section 9 of the Act, the mere circumstance that it falls under a different head or is to be regarded as a different source would not, in my opinion, exclude it from consideration. It is not always clear whether a particular income should be entered under one head or another. I know of no limits which can be laid down so as to prejudice the question whether any particular receipts have or have not escaped assessment and I am not prepared to say that it is never open to an assessee to show, for this purpose, that his income under one head must be reduced if his income under another head is to be enhanced. In the case before us, however, it appears to be clear enough that the extent to which the zemindari collections are exempt from income-tax as being agricultural income is not affected by, and has no bearing upon, the question of the profits of the business of money-lending, or the question of the

annual value of the assessee's buildings and land appurtenant thereto of which they are the owners. In any event, the question which has been referred to us and argued before us assumes this.

On this footing I am unable to say that the language of section 34 points to an intention to give to the assessee a right to re-open the whole assessment before being rendered liable to further tax. It is not for the Court to determine whether the administrative inconvenience entailed by such a right would be much or little, or whether it would afford any sufficient reason for refusing to the assessee a right to re-open the whole matter. Nor is it for the Court to consider whether there is any real injustice or inconvenience in refusing this right to an assessee who has failed to make a return. Such considerations are questions of policy and debatable as such. As a matter of the true construction of this section it appears to me that if the legislature had meant to say that if in any case it appears to the Income-tax Officer that an assessee has been assessed upon too low a figure or at too low a rate, the Income-tax Officer may issue a fresh notice under section 22 (2) and may proceed to reassess such assessee afresh, the language employed would have been noticeably different from that which we find in the present section.

It is clear that the initial duty of the Income-tax Officer is merely to assess the income which has escaped. If this be right then I think that it would require express words to confer on the assessee a right to re-open other and unconnected matters. It is true that there is no express reference in the section to Sources or Heads of income. But these will usually come into the question in favour of the assessee since the assessment order will usually assess him at a lump sum under each head and in any case in which such an assessment has been made in default of a return of income or of production of accounts the assessee will thus be able to contest the whole assessment made under that head if it is afterwards said to be insufficient.

It appears to me, therefore, that the question which has been referred to us must be answered against the assessee, but I am not altogether satisfied with the form in which it is expressed. In my opinion it is always open under section 34 to an assessee to show in any way he can that the income, profits or gains alleged to have escaped assessment have not in truth and in fact escaped assessment, and for this purpose it is not true that income, profits or gains have necessarily escaped assessment because they have not been assessed under the right head. But if it is once shown that income has escaped assessment, the assessee cannot under section 34 resist proceedings to assess it merely by showing that other income, profits or gains have been assessed at too high a figure.

The assessee must pay the costs of this reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(373) IN THE HIGH COURT OF JUDICATURE AT LAHORE.

Before Justice Sir Alan Broadway, Kt., and Mr. Justice Currie.

(14th May, 1930).

Nawalkishore Kharaitilal, Firm

.. Assessee.*

The Commissioner of Income-tax, Delhi

*Indian Income-tax Act (XI of 1922) Secs. 23 (4), 42, 43 and 66 (3)—
Interest paid to non-resident—Assessment on resident debtor as agent of non-*

resident after service of notice—Assessment as no return cases—Reference to High Court, right to ask for.

The assessee in the course of their assessment for 1923-24 claimed a deduction of interest paid by them to a non-resident creditor and on the claim being allowed an assessment of the interest amount was made on them as agents of the non-resident under Secs. 42 and 43 of the Act, after giving them an opportunity to show cause under Sec. 43. For the succeeding years 1924-25 and 1925-26, notices under Sec. 22 (2) addressed to the non-resident were served on them and on non-submission of returns, assessments were made on them as agents on the interest amounts credited in their books in favour of the non-resident, the cases being treated as 'no return' cases. After an unsuccessful application under Sec. 27 to re-open the assessments, appeals were preferred to the Assistant Commissioner who dismissed them. On an application under Sec. 66 (3),

HELD, (1) that the cases were rightly treated as no 'return cases' and consequently the assessee had no right to ask for a reference, the fact that appeals were entertained by the Assistant Commissioner being immaterial and

(2) that the assessee not having asked for a fresh order or decision under Sec. 43, were rightly regarded as agents within the meaning of Secs. 42 and 43 for the years 1924-25 and 1925-26.

Application [Civil Miscellaneous No. 316 of 1928] under Sec. 66 (3) and (4) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Delhi, to state a case for the opinion of the Court.

Dr. Moti Sagar, for the Assessee.

Abdul Rashid, Additional Government Advocate, for the Crown.

JUDGMENT.

BROADWAY, J.:—This matter has been before the Court on a former occasion when a Division Bench consisting of Mr. Justice Bhide and myself returned the case to the Commissioner of Income-tax, Delhi, for such action as he might deem necessary. In the order passed by us on the 27th June 1927, the facts are detailed; briefly, the firm of Messrs. Nawal Kishore Kharaiti Lal carrying on business as Jewellers in Delhi had dealings with one Banji Lal of Jaipur. Banji Lal advanced large sums of money to Nawal Kishore Kharaiti Lal and received from them very substantial sums of interest. In the course of the assessment of income-tax on Nawal Kishore Kharaiti Lal in 1922-23 they claimed that this interest which had been credited to Banji Lal at Delhi should be allowed them as business expenses. Their request was granted and then in 1923-24 Banji Lal was assessed to income-tax on the amount of interest credited by Nawal Kishore Kharaiti Lal in their account books. Nawal Kishore Kharaiti Lal were called upon to pay the amount assessed and they raised various objections, the principal ones being (1) that they were not the agents of Banji Lal under sections 42 and 43 of the Income-tax Act and, secondly, that they had not been given proper opportunity of making a return. These objections were disallowed after the objectors had been given an opportunity under section 43 of the Income-tax Act to satisfy the authorities that they should not be regarded as Banji Lal's agents. Against that decision they preferred various appeals and finally attempted to get the Commissioner of Income-tax to make a reference to this Court under section 66 (2). This reference was, however, dismissed as barred by time. In the interval the authorities endeavoured to assess Banji Lal through their agents for the years 1924-25 and 1925-26. A certain amount of confusion has arisen owing to the fact that instead of filing separate objections and separate applications with regard to these two years, the firm of Nawal Kishore Kharaiti

Lal has thought fit to combine their attack on the assessment for these two years in one application which should not have been allowed by the Income-tax authorities.

A reference was made by the Commissioner of Income-tax, Delhi, but was in such vague terms that it was found necessary on the 27th June 1927 to return the papers to the Income-tax Commissioner leaving it open to him to decide whether he would make a further reference or not.

On a careful consideration of the situation the Commissioner of Income-tax decided that no case had been made out for a reference to this Court and he accordingly refused to make one. Nawal Kishore Kharaiti Lal have, therefore, come up to this Court under section 66 (3) of the Income-tax Act and, through Dr. Moti Sagar, have asked us to direct the Commissioner of Income-tax to refer certain questions of law to this Court.

One of the points taken was that the Commissioner of Income-tax had no right to refuse to make a reference. A perusal of the judgment of this Court dated the 27th June 1927 makes it quite clear that it was intended to give him a free hand in this respect. Now, it has been held by the Income-tax Officer, Assistant Commissioner and all the Income-tax authorities that both assessments were made under section 23 (4), that is to say, that in both years the cases were treated as 'no return cases' and it has been admitted that if these are 'no return cases,' then the petitioners have no right to ask for the reference prayed for.

It has, however, been urged that in neither of the years was the case a 'no return case.' Now, turning to the year 1925-26, we find that the petitioners credited Banji Lal with a sum of Rs. 63,142 as interest. This sum, it has been stated, has been allowed to the petitioners as their business expenses. On the 14th December 1925, a notice was sent, under section 22 (2), under a registered cover, addressed to Seth Banji Lal care of the petitioners. The petitioners re-directed this to Jaipur and that we are asked to believe for some reason or other was never delivered. On the 27th January 1926, the same notice was sent under registered cover to the petitioners. This they received on the 28th January 1926, but as the declaration form, inside the registered cover, was addressed to Banji Lal, the petitioners returned the form in its blank state to the Income-tax Officer who subsequently assessed Banji Lal through the petitioners treating it as a 'no return case.' Against this an appeal was lodged to the Assistant Commissioner who dismissed it as incompetent. In these circumstances, in my judgment, the case for the year 1925-26 was clearly a 'no return case' and admittedly this application must fail *qua* that year.

Turning now to the year 1924-25, it appears that a declaration form was sent on the 30th or 31st July, 1924, under section 22 (2). This was addressed to Banji Lal through the petitioners. It was returned by the petitioners with a suggestion that it should be sent to Jaipur. On the 13th October the declaration form was re-sent to Banji Lal care of the petitioners and under a registered cover which was again returned. On the 27th March 1925, the Income-tax Officer held that this was a 'no return case' and as the amount shown in the petitioners' books as having been credited to Banji Lal was Rs. 30,000, the assessment was made on that figure, and the petitioners as agents were called upon to pay. Thereupon the petitioners moved the Income-tax Officer under section 27 of the Income-tax Act. Meeting with no success they attempted to appeal to the Assistant Commissioner in spite of the fact that the proviso to section 30 (1) clearly lays down that no appeal is competent. The Assistant Commissioner in dealing with this appeal pointed out that the Income-tax Officer had seen no reason to revise his assessment and that he, the Assistant Commissioner, also failed to see any reason to do so. The appeal was accordingly dismissed.

It has been urged by Dr. Moti Sagar that because the Assistant Commissioner 'entertained' the appeal, therefore, the order was appealable. Section 30 appears to me to be perfectly clear on the point. It provides for an appeal by an assessee who objects to the amount or the rate at which he is assessed under section 23 or section 27, etc. The proviso runs that no appeal shall lie in respect of an assessment made under sub-section 4 of section 23, or under that section read with section 27. It seems to me that the present case comes within this proviso and it is one of those cases which fall in the category of an assessment made under sub-section 4 of section 23 read with section 27. In my judgment, therefore, the assessment for this year was also a 'no return case', the appeal to the Assistant Commissioner was incompetent and the mere fact that the Assistant Commissioner in dismissing the appeal did not say that it was incompetent does not affect the case. Whether there is or is not a question of law involved in this matter is, therefore, immaterial and could not be discussed.

Before concluding I would add, in the present case the firm of Nawal Kishore Kharaiti Lal were deemed to be agents after due notice and hearing as provided by section 43. It has been urged that that decision only related to the year 1922-23. It has, however, been pointed out by the learned Government Advocate that in all the subsequent proceedings relating to the years 1924-25 and 1925-26 Nawal Kishore Kharaiti Lal never asked for a fresh order or decision after a hearing under section 43 and, in these circumstances, I think that they have rightly been regarded as agents within the meaning of sections 42 and 43 of the Income-tax Act.

I would, therefore, dismiss this petition and decline to issue the mandate as prayed for. Parties will bear their own costs.

CURRIE, J.:—I agree

(374) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Bennet.

(16th May, 1930).

Radhey Lal Balmukand

.. Assessee.*

v.

The Commissioner of Income-tax, United Provinces. .. Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 13, 22, 23, and 66—Separate return notices, issue of—Joint assessment as Hindu joint family—No opportunity to adduce evidence re separateness—Accounts not disclosing true income—Assessment without disclosing basis therefor, Legality of—Reference to High Court—Questions not raised before Income-tax authorities—Reference Fee.

Where during the course of assessment proceedings after submission of return in pursuance of three separate notices under Sec. 22 (2) the Income-tax Officer came to the conclusion from certain statements recorded by him that the three proposed assesseees were really members of a Hindu joint family and made a joint assessment on them as such, without informing them of the proposed joint assessment or giving them an opportunity to adduce any evidence in support of their separateness,

HELD, that there was material irregularity and disregard of the provisions of Secs. 22 and 23 invalidating the assessment.

* (1930) 52 All. 991; (1930) A. L. J. 1548; A. I. R. (1931) All 23.

Where the Income-tax Officer assessed the income from business at a certain figure without stating the basis therefor, the assessee's account books not furnishing any proper clue of the actual income,

HELD, that Sec. 13 did not authorise the Income-tax Officer to act arbitrarily and without any evidence and the assessment not disclosing the basis or method adopted by the Income-tax Officer was illegal.

On a reference under Sec. 66 of the Income-tax Act only such points of law should be considered by the High Court as were already before the Officers of the Income-tax Department.

The sum of Rs. 100 deposited under Sec. 66 (2) is part of the costs of the reference to be taxed as such.

Case [Miscellaneous Case No. 37 of 1930] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces in compliance with the order of the High Court dated 31st January, 1930.

CASE.

This statement is submitted in accordance with the instructions of the High Court in their order under section 66 (3) of the Income-tax Act, dated January 16, 1930, amplified in the letter of the Deputy Registrar of the High Court, No. 2429, dated January 31, 1930.

2. The demand for a reference in this case includes various matters which are so diverse that it will be probably for the convenience of the Hon'ble Judges of the High Court if, in accordance with rule 11 of the rules framed by the High Court of Judicature at Allahabad, in their Notification No. 606/35, dated February 16, 1925, this reference is divided into two parts, the first relating to the question whether the assessment of a Hindu undivided family with reference to certain businesses is correct, and the second to points arising in the course of the assessment of income, profits and gains from various sources.

PART I

3. In the year 1927-28 an assessment to income-tax was made for the first time in respect of three businesses carried on in Agra under the name and style of—(i) Radhey Lal Balmukand, (ii) Balmukand, and (iii) Radhey Lal Shyam Lal. The businesses were treated as if they belonged to three different persons and three assessments were made as the inner relationship of the proprietors of the three businesses does not appear to have attracted the close attention of the then Income-tax Officer who accepted a statement by Radhey Lal regarding the separate nature of the businesses. Messrs. Radhey Lal Balmukand were treated in their assessment as an unregistered firm. The assessment in the other two cases was made as if the owners of the businesses were Hindu undivided families. This position was maintained in 1928-29 at the time when notices were issued, under section 22 (2) of the Income-tax Act, calling for a return of income, and three notices under that section were issued in the names of the three proprietors of the three businesses. Before, however, the assessment was made, another Income-tax Officer received the information that although there were three businesses they really belonged to a Hindu undivided family. He proceeded to make enquiries and found that Balmukand and Radhey Lal were brothers and that Shyam Lal was the son of Radhey Lal and that no partition in the family had taken place. He recorded the statements of Balmukand and Radhey Lal, a translation of which is attached in Appendices A* and B*. In his statement Balmukand said that he and Radhey Lal were brothers and members of a Hindu

undivided family, that whatever income was earned by Radhey Lal and himself was thrown into a common stock and credited in the accounts of the firm of Radhey Lal Balmukand, that no partition of income or property had taken place between Radhey Lal and himself, that Shyam Lal was the son of Radhey Lal and lived with his father jointly, that he carried on no business in his own name or in the name of Radhey Lal or Shyam Lal but all the business was carried on in the name of Radhey Lal Balmukand and Radhey Lal Shyam Lal and not in any other name, and that they owned jointly two shops in Kinari Bazaar and a house in Namak Mandi. Radhey Lal in his statement said that Balmukand was his brother and Shyam Lal was his son, that no partition had taken place as between Balmukand and himself on the one hand or between Shyam Lal and himself on the other hand, that no transactions in Agra were entered into in the name of Radhey Lal Shyam Lal, and that all transactions at Agra carried on by Radhey Lal Shyam Lal were in the name of Radhey Lal Balmukand, that the transactions at Bombay took place in the name of Radhey Lal Shyam Lal and finally that he could not assign any reason for the fact that all the transactions at Agra carried on by Radhey Lal Shyam Lal were carried on in the name of Radhey Lal Balmukand. In view of these categorical statements the Income-tax Officer found that all the three businesses belonged to a Hindu undivided family and assessed the family accordingly.

An appeal against this decision was filed before the Assistant Commissioner of Income-tax on the following grounds (*vide* copy of petition of appeal in Appendix C)*:—(a) “A finding on this point having already been finally arrived at by the Income-tax Officer last year, the matter should be deemed to have been concluded, and the Income-tax Officer had erred in coming to a different finding now.” (b) “Though Radhey Lal and Balmukand are undoubtedly owners of the firm of that name and their business is undivided yet they do not form a joint Hindu family according to law and Hindu Shastras.” (c) “The books themselves prove that Radhey Lal and Balmukand are not members of a joint Hindu family and that their expenses, profits, and losses are separate, though some of their ancestral property is in their possession as co-owners.” (d) “It is admitted that Radhey Lal and his son Shyam Lal do constitute a joint Hindu family.”

The Assistant Commissioner held that as the assessee had admitted that they were joint the Income-tax Officer could not but assess the businesses as those of a Hindu undivided family. He further refused to take into consideration a will which was produced before him during the arguments on behalf of the assessee, the ground for his refusal being that he would not accept evidence which had not been produced before the Income-tax Officer. The Commissioner of the time held that since the matter was clinched by the statement of the assessee no case arose for the decision of the High Court. He further held that there was no need to state a question of law on the point whether the action of the Income-tax Officer in the preceding year constituted *res judicata*.

4. In the opinion of the present Commissioner the points of law which arise are:—(1) Was there evidence on which the Income-tax Officer could come to a finding that the businesses were owned by a Hindu undivided family? and, (2) Did the action of the Income-tax Officer in the year 1927-28 when he treated the three businesses as owned by a firm and two Hindu undivided families, respectively, debar the Income-tax Officer in 1928-29 from treating the businesses as belonging to a Hindu undivided family in the circumstances which have been narrated?

5. A copy of paragraphs 1—4 was furnished to the advocate of the assessee for his opinion in accordance with the principle embodied in rule 7 of the

* Not printed.

High Court rules cited in paragraph 1. His reply is contained in Appendix F.* The statement of the facts in the foregoing paragraphs is accepted but the petitioner desires to raise the following three points of law in addition to those stated in the foregoing paragraph:—“(i) As no evidence was summoned from the assesseees on the point of jointness or separation and no notices having been issued to them, could the Income-tax Officer record the finding that the assesseees were members of a joint Hindu family? (ii) Was the Assistant Commissioner justified in refusing to accept the will in evidence? (iii) The Income-tax Officer having found in previous years, when the point about the separation and the jointness was specifically raised and when the will of the assesseees’ ancestors was produced in evidence, could the Income-tax Officer on the evidence before him come to a finding that the businesses were owned by a Hindu undivided family?”

The Commissioner is of opinion that the first question is covered by the first question in paragraph 4. The Income-tax Officer directed his mind to the question and made enquiries from the persons who were most likely to know, *i.e.*, the members of the family themselves. In the course of this assessment the will was not produced although it was clear from the fact that evidence was being recorded on the point that the question of the existence or otherwise of a Hindu undivided family was in issue. The Commissioner, therefore, does not add this question to those stated for the consideration of the High Court.

The second point was not raised in the petition to the Commissioner under section 66 (2), asking him to state a reference to the High Court, and is therefore time-barred. The Commissioner is unable to state this question.

The third point is based on an error of fact. As already stated in paragraph 3 above, the businesses were treated in the year 1927-28 as belonging to entirely different persons. In March, 1929, after the assessment for the year 1928-29 (now in issue) was completed, the Income-tax Officer took proceedings under section 34 of the Income-tax Act with reference to income which he considered to have escaped assessment in the year 1927-28. In the course of these proceedings, that is to say, on April 16, 1929, a petition was filed before the Income-tax Officer in which the following paragraph occurs:—“I have in obedience to your honour’s order brought to-day not only all the accounts summoned by Your Honour which had however been rejected previously—but also all the books which will establish conclusively that we, Radhey Lal and Balmukand, who carry on business jointly had separated more than 15 years back. We have also brought the original will executed by our father in 1912—a registered document—which shows unmistakably that we had separated even before that.”

The point raised in this petition, which, it may be emphasised, is subsequent to the date on which the Income-tax Officer made the assessment now in question, has not yet been decided because the file has been in constant requisition with reference to the proceedings which have resulted in the present case. The will was not produced either during the assessment of 1927-28 or the assessment of 1928-29 so that, so far as the record shows, it is incorrect to say, as in the paragraph quoted above, that the will of the assessee’s ancestor was produced in evidence to prove the separation of the members of the family. This being so, the question as stated does not arise and the Commissioner is unable to submit it for the decision of the High Court.

6. In the opinion of the Commissioner the answer to the first question in paragraph 4 is in the affirmative and to the second question in the negative.

PART II.

7. This portion of the reference deals with the income assessed and the manner of assessment. Five points have been raised in the petition to the High Court under section 66 (3)—(Copy attached in Appendix D)*—

- (i) Whether in the case of the business known by the name of Radhey Lal Shyam Lal the Income-tax Officer was right in excluding a certain loss incurred in the business of another firm?
- (ii) Whether in the case of the business known by the name of Radhey Lal Balmukand the Income-tax Officer was entitled to take an imaginary figure of profits of Rs. 45,000?
- (iii) Whether in the case of the business known by the name of Balmukand, the Income-tax Officer was justified in assuming an income of Rs. 1,000?
- (iv) (a) Whether the Income-tax Officer had power to reject the accounts of one business when he had accepted the accounts of another?
- (b) Whether he had power to reject the accounts of the business mentioned without giving any reason and without giving the assessee "an opportunity to remove the doubt of the Income-tax Officer and to substantiate his books"?
- (v) Whether the procedure adopted by the Income-tax Officer was in accordance with the law?

The second part of the fourth question appears to be the same in substance as the second, and the fifth point seems to be tautologous. Reference to them will not be made again. The other points will be dealt with in order, the facts being first recited.

8. In the case of the business styled as Radhey Lal Shyam Lal the assessment was based on the accounts which were accepted as correct, although not free from objection. But a loss which had been incurred in a business carried on by the assessee in partnership with Chandmal Dhirajmal was disallowed. That business related to the year 1982-83 Sambat, and resulted in a loss, but the assessee carried that loss to his accounts in the year 1983-84 Sambat. Since the loss definitely occurred in a previous year the Income-tax Officer held that it could not be carried forward so as to be set off against the profits of the period assessed in 1928-29. The assessee claimed that although the loss occurred in that year he could not bring it to account before the accounting period now under consideration and that therefore the loss should be allowed.

There is no order of the Assistant Commissioner on this point because it was not raised in appeal—(copy of petition attached—Appendix C).*

9. The business known as Radhey Lal Balmukand consisted of the gold and silver bullion and gold and silver ornaments. The sales amounted to over Rs. 17 lakhs. But the accounts showed a profit of only Rs. 5,298. The profit was so small when compared with that obtained by other persons carrying on similar business that the Income-tax Officer directed his attention to a close analysis of the accounts. He describes the result of his examination in the following words:—

"In this *khata* gold and silver bullion, old metal and ornaments are dealt with so that it is impossible to analyse the account. Why the assessee has maintained one *khata* for gold, silver, old metal and ornaments I am unable to understand, for it is contrary to the practice of all other *sarrafs* without exception.

* Not printed.

An attempt was made at analysis but it was found that the assessee had no details in respect of several items against each of which there is merely a note gold or silver. The *pucca rokar* and even the *kacha rokar* have no details. In the first instance, there being no weights, it makes analysis absolutely impossible and secondly as has been pointed to the assessee there is nothing to show that such entries are not bogus. It is alleged by the assessee that the total of such items would not exceed two lakhs but that makes no material difference for if the assessee made an entry of Rs. 50,000 as purchases when in reality he had not purchased any gold, silver or ornaments the profit would automatically be reduced by that amount. Under the circumstances I reject the accounts."

"Apart from this I have come across two items that were noted from the books of another assessee which do not find place in the assessee's accounts."

He thereupon proceeded to frame the assessment to the best of his judgment and the figure which he took, shows that he was influenced by the volume of the transactions disclosed in the books. The view of the Assistant Commissioner is contained in the following extract from his appellate order:—

"I now come to the question whether the Income-tax Officer has been right in having rejected the profits relating to the Mal Khata. As already mentioned the sales of the assessee on account of gold and silver bullion and ornaments came to Rs. 17,24,764. They worked out a profit of Rs. 5,298 on these huge sales. The Income-tax Officer could not satisfy himself as to the accuracy of these profits as there were no details of the weights and the rates of purchases and sales, and therefore rejected the profits worked out. He has also noted that there were two items he had come across in the books of another assessee which did not find place in the assessee's accounts. It has been rightly pointed out that the Income-tax Officer should have noted the two items in order to enable the assessee to meet the objection. The point, however, is not very material as the main ground on which the accounts have been rejected is that it is impossible to analyse the books in detail in order to satisfy oneself fully as to the profits worked out. I have ascertained from the assessee themselves, and they have admitted, that their retail sales are about half the total sales and that they also purchased old ornaments worth about two lakhs. If this is so, it is difficult to understand how the assessee could have made such low profits. I have found that, in some cases, assessee dealing in gold and silver ornaments have made as much as 10 per cent. profits on their entire sales including gold and silver bullion. If the sales of the assessee include as much sale of old ornaments as two lakhs, I have little doubt that either the sales have been understated or the price of such ornaments has not been correctly put down. It may also be noted that at the last assessment the books of account were found to be absolutely unreliable as is clear from the assessment orders of the then Additional Income-tax Officer, dated March 3, 1928. In that year it was found that the assessee, who does considerable speculation business also, has neither entered all his speculation profits nor entered all his sales or purchases. In these circumstances the Income-tax Officer has not been wrong in having rejected the books when he could not feel satisfied as to the accuracy of the profits returned. I have also considered the question whether the estimate of Rs. 45,000 as the profit of this business, is reasonable or not. I think that, in view of the enormous retail sales, and the sale of old ornaments worth about Rs. 2,00,000, which decidedly carry much greater profits than the sale of ordinary silver and gold bullion, the profits estimated are not excessive."

10. As regards the business known by the name of Balmukand the person assessed under that name in 1927-28 was found to have received Rs. 1,000 on account of his share of interest from Kalyan Das Kapur Chand. He had, however, only brought to account a sum of less than Rs. 600 and explained the discrepancy by saying that he had spent the balance and so had not brought it to

account. In the assessment now under consideration the Income-tax Officer remarked that the interest income of this portion of the business had not been accounted for in the return while accounts were denied. The Income-tax Officer, therefore, took Rs. 1,000—the same sum as had been assessed in the preceding year. In appeal the Assistant Commissioner refused to intervene. This point was not specifically raised before the Commissioner in the demand for a reference to the High Court under section 66 (2). A copy of this petition is attached, Appendix E.*

11. With reference to the first part of the fourth question it is a fact, as stated in paragraph 8 above, that the Income-tax Officer accepted the results shown in the accounts although they were not free from objection; he was influenced in his action by the fact that the amount of business in this concern was small. This point was not raised in appeal and was therefore not the subject of an appellate order by the Assistant Commissioner.

12. Since the points dealt with in paragraphs 8 and 11 were not raised in appeal and were therefore not the subject of an appellate order, no reference to the High Court can, under section 66 (2) of the Income-tax Act, be claimed. The assessee also failed to claim a reference on the third point (paragraph 10 above) within the period of limitation prescribed under section 66 (2) of the Income-tax Act and the present demand, therefore, under section 66 (3) that the question be decided by the High Court is time-barred. No questions on these points accordingly are suggested for the consideration of the High Court.

13. As regards the second point (paragraph 9 above), which is the most important, the Commissioner feels considerable doubt whether any question of law arises. Section 13 of the Income-tax Act provides that, if the Income-tax Officer is of the opinion that the method of accounting employed by the assessee is such that the income, profits and gains of an assessee cannot be deduced therefrom, the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine. Whether or not the Income-tax Officer can deduce the profits or gains of a business from account books which are produced before him is a question of fact. The question is for the judgment of the Income-tax Officer and does not seem to come within the purview of the High Court. Any point of law, however, can only concern the reasonableness of the grounds on which the Income-tax Officer acts and the Commissioner would suggest that, if any question of law does arise, it is in the form—Was the condition of the account books such as to justify the Income-tax Officer in holding that the income, profits and gains of the assessee could not be deduced from his books?

14. A copy of the paragraphs now numbered 7—13 was furnished to the advocate of the assessee whose reply is contained in Appendix F,* already referred to. He is of opinion that the statements in the concluding sentence of paragraph 8 and (as the Commissioner understands) in the penultimate sentence of paragraph 10, that the points were not raised in appeal or before the Commissioner when the application under section 66 (2) of the Income-tax Act was presented, are incorrect. The Commissioner, however, has perused the petitions again (*vide* Appendices C* and E*) and is of the opinion which he originally expressed. The petitioner also suggests that, although the Commissioner holds that he cannot state the points discussed in paragraphs 8, 10 and 11 for the consideration of the High Court, the points should be stated for the consideration of the High Court in case his opinion is not accepted. This, in view of that opinion, the Commissioner finds himself unable to do.

The assessee also asks that the following questions may be referred to the High Court:—

- (i) Was the Income-tax Officer justified in applying section 13 of the Income-tax Act without taking proceedings under section 23 (3)?
- (ii) Was the Income-tax Officer bound to take proceedings under section 23 (3) before applying section 13 of the Income-tax Act?
- (iii) Had the Income-tax Officer any power to assess on an imaginary figure under sections 13 and 23 (3) of the Income-tax Act?
- (iv) Could the Income-tax Officer fix an imaginary figure for assessment without laying down the basis for his computation?
- (v) That the Income-tax Officer having accepted that the method of accounting was mercantile and that being the method adopted by the assessee and he not having found that any particular item of account was bogus, could the Income-tax Officer under section 13 assess the tax on an imaginary figure?

The first question was not raised on appeal and therefore the Commissioner is unable to state it for the consideration of the High Court. The second and third questions are in effect the same as those numbered (iv) (a) and (b) in paragraph 7 above. The fourth question is based on an error of fact. The Income-tax Officer, it is true, did not include in his order his detailed calculations regarding the profits of the business, but he was clearly influenced in the amount which he assessed by the sales of over Rs. 17 lakhs which he found in the books of the assessee. The question of law as propounded by the petitioner does not appear to arise.

The fifth point, so far as the Commissioner understands it, is almost the same as the fourth. It was incumbent on the Income-tax Officer to frame an assessment. Since for definite reasons he had rejected the books of the assessee he was bound to come to a conclusion to the best of his judgment. The facts on the record show in effect how his judgment has been exercised and no point of law appears to emerge.

15. The only question which in the opinion of the Commissioner can arise is that stated at the end of paragraph 13. If the High Court holds that the question does arise the Commissioner desires to say that in his opinion the answer is in the affirmative.

Kunzru, for the Assesseees.

Bajpai, for the Crown.

JUDGMENT.

This matter has arisen out of an application made to this Court by three assesseees asking this Court to call upon the Commissioner of Income-tax, United Provinces to state a case, he having refused to state one when applied to for the purpose by the applicants. The Commissioner of Income-tax has now stated a case and we have to see what are the questions of law that arise for determination by this Court.

The learned Government Advocate has placed before us an unreported judgment of a Full Bench of the Madras High Court* delivered on 20th of January 1930, as an authority for the proposition that the High Court would not consider any point of law that was not raised either before the appellate Officer or the Commissioner himself by the assesseees. We have no reason to differ from

* Since reported as *S.A.S. Subbiah Iyer vs. Commissioner of Income-tax, Madras* 4 I.T.C. 345.

what was laid down in that case, and we think it but right that only such points of law should be considered by the High Court as were already before the Officers of the Income-tax Department.

To find out what are the real points of law that arise in this case the following facts have to be stated. One Bankéy Lal had several sons. We are concerned with only two, namely Radhey Lal and Balmukand. Radhey Lal's son is Shyam Lal. There were three persons who were assessed with income-tax in the year previous to the year in question—(1) Balmukand, (2) Radhey Lal Shyam Lal and (3) Balmukand Sarraf. They were assessed separately to income-tax. In the year in question, that is to say, in the year 1928-29 three separate notices were issued on 1st of April 1928 to the three persons aforesaid, under section 22 (2) of the Income-tax Act, calling on them to make a return of their respective incomes. They submitted returns and they also produced their account books as desired by the Taxing Officer. The Taxing Officer thereupon proceeded to assess them with income-tax. He, however, at some stage or other made up his mind to find out whether the three proposed assesseees should or should not be assessed jointly as members of a joint Hindu family. He accordingly at different dates examined Radhey Lal and Balmukand. From statements made before him the Income-tax Officer came to the conclusion that the three proposed assesseees were really members of the same joint Hindu family. He taxed jointly with a certain amount of tax. The first point that is urged before us is that this procedure was wrong in as much as the assesseees were never given an opportunity to contest and disprove the allegation that they were members of a joint Hindu family and were liable to be taxed jointly.

In actually assessing the three persons mentioned above the Income-tax Officer examined the account books produced before him. He proceeded, according to his own assessment order, under section 23 (3) of the Income-tax Act. That section lays down that where a return has been made and the Income-tax Officer has reason to believe that the return is incomplete or incorrect, he shall call upon the assessee to produce evidence and after hearing all the evidence that may be liable to be examined the Officer will make an assessment. It is to be noted that the Income-tax Officer was not professing to proceed under section 23 sub-section (4), which allows, in certain cases of default by the assessee, the Income-tax Officer to make an assessment "to the best of his judgment."

The Income-tax Officer having found that some of the books of the assesseees were not clear as regards the income derived by the owners thereof from dealing in precious metals, assessed the income at Rs. 45,000. He did not state what was the basis of his computation.

The assesseees raised the point, *viz.*, that the Income-tax Officer was not justified under the law in making what was virtually an assessment to the best of judgment.

The assesseees raised two other points. One is about a sum of Rs. 772, a sum said to have been the amount of a loss and another sum of Rs. 1,000, the estimated income from interest payable to Balmukand. As regards the amount of Rs. 772, we do not consider it at all, because in the appeal that was filed against the assessment made by the Income-tax Officer no complaint was made as to the exclusion of this sum from the account.

As regards the sum of Rs. 1,000, we also exclude it from our consideration, because on the admitted facts there was no account book produced by Balmukand and the previous year's income on the head was Rs. 1,000. Thus there was certainly a basis on which the Income-tax Officer could estimate the income for the year in question.

We now proceed to consider the points of law that have been stated above. It is not denied that the assesseees were never told that they were going to be assessed as members of a joint Hindu family. The notices that were issued to them indicated that they were going to be assessed separately. The notices never stated that they should be assessed jointly and, therefore, no "issue," in the ordinary sense of the word, ever arose between the Income-tax Officer on the one hand and the assesseees on the other, as to the jointness or separation of the family. If it be true, as has been stated, that the Income-tax Officer came to know that the assesseees were really members of a joint Hindu family, it was his duty, in the name of fair play, to tell the assesseees that he proposed to assess them jointly as members of a joint Hindu family and to call on them to show cause why he should not proceed accordingly. As already stated, the procedure that he had adopted was to assess the assesseees separately. The mere fact, that the statements of Radhey Lal and Balmukand taken, at different dates, indicated that they were members of a joint Hindu family along with Radhey Lal's son Shyam Lal, did not justify the Income-tax Officer in the procedure that he adopted. From the fact that the assesseees were not called upon to adduce any evidence in support of their case of separation they were unable to produce any evidence. When the matter went up in appeal before the Assistant Commissioner, the assesseees wanted to produce a copy of a registered will, alleged to have been executed by Bankey Lal, the father of Radhey Lal and Balmukand. But that Officer refused to accept it on the ground that it had not been tendered before the Income-tax Officer. The assesseees, however, never had any chance to produce the document before the Income-tax Officer. We are of opinion that there was a material irregularity and disregard of the procedure as laid down in sections 22 and 23 of the Income-tax Act, in assessing the applicants without giving them any information of the proposal to do so and without permitting them to adduce evidence in support of their contention. This is our answer to the first question.

As regards the second question, *viz.*, whether the Income-tax Officer was justified in fixing the income of the assesseees at the sum of Rs. 45,000, we are of opinion that what the Income-tax Officer virtually did was to act under sub-section (4) section 23 of the Income-tax Act. If it was true, as we assume that it was true, that the assesseees' account books did not furnish any proper clue of the actual income, it was open to the Income-tax Officer to accept such evidence as he might get for the purpose of finding out the true income. He does not in his order state any basis at which he arrived at the figure of Rs. 45,000. Section 13 of the Income-tax Act did not authorise him to act arbitrarily and without any evidence. If the account books did not furnish any method of computation of the profits, he had to employ such methods and such basis as appealed to him as the best, but he had to employ some "basis" or method as he thought fit. But he did not employ any method at all. We are, therefore, not in a position to say that he acted legally in the matter. Our answer, therefore, to this question is that the assessment was illegal having regard to the provisions of section 23 sub-section (3) of the Act.

Let a copy of this judgment under the seal of the court be sent to the Commissioner of Income-tax. As the assesseees have substantially succeeded, they will have their costs of this reference. The learned Government Advocate is entitled to a day's fee which is Rs. 250. He will certify payment to him within the prescribed period.

Mr. Kunzru has argued that the costs of the reference which have been awarded to the applicants should also include the sum of Rs. 100, deposited by his clients for a reference under sub-section (2) of section 66 of the Income-tax Act. We have heard the learned counsel for the Government on the point. We can regard the amount of Rs. 100 deposited by the assesseees only as a part of the

costs of the reference. All fiscal enactments must be construed in favour of the subject and it cannot be said that if an assessee has not been properly taxed and if he succeeds on a reference in the High Court, yet whether he succeeds or loses, he must lose a sum of Rs. 100, simply because an Income-tax Officer has chosen to make an assessment. We think, therefore, that the sum of Rs. 100 is a part of the costs of the reference, and we, therefore, direct that it will be taxed as such.

(375) IN THE HIGH COURT OF JUDICATURE AT RANGOON.

Before Mr. Justice Carr and Mr. Justice Cunliffe.

(19th March, 1930).

E. M. Chettyar Firm

Assessees.*

vs.

The Commissioner of Income-tax, Burma

Indian Income-tax Act (XI of 1922) Sec. 66 (4) and (5)—Commissioner confirming enhanced assessment by Assistant Commissioner—High Court directing Commissioner to consider Assistant Commissioner's grounds for enhancement—Commissioner's finding as to sufficiency of ground—Reference to High Court, if lies—Reasons for finding, non-stating of—Jurisdiction of High Court.

On a reference to the High Court arising out of an order of the Commissioner of Income-tax in an appeal confirming the enhancement of assessment by the Assistant Commissioner, the Court was of opinion that the Commissioner should call upon the Assistant Commissioner to give his grounds for enhancement and should consider as an appellate tribunal whether the enhancement was justified. The Commissioner after calling for a report from the Assistant Commissioner found without detailing reasons that there were ample materials for the enhancement. On the Commissioner's refusal to state a case on the ground that his order was a revisional order passed under Sec. 66 (5) of the Act and not one under Sec. 31 or 32, the assessee applied to the High Court under Sec. 66 (3).

HELD, that the High Court intended to proceed under sub-section 5 and not sub-section 4 of Sec. 66, the Commissioner to deal with the case as a referred appeal without further recourse to the Court and that there was no question of law for a reference.

CAR, J.:—The High Court has no jurisdiction to consider the findings of fact arrived at by an Income-tax authority and it is immaterial whether the grounds stated for these findings are sound or unsound, or whether no reasons at all have been stated.

Application [Civil Miscellaneous Application No. 148 of 1928] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Burma to state a case for the opinion of the High Court.

Faucar, for the Assessees.

Eggar, for the Crown.

JUDGMENT.

CUNLIFFE, J.:—This is an application for mandamus against the Commissioner of Income-tax, Rangoon, under section 66 (3), Income-tax Act. The petitioners, the E. M. Chettyar concern of Moulmein, require the Commissioner to state a case in law by reason of a direction given by a Bench of this Court in an earlier reference between the same parties reported in *E. M. Chettyar Firm vs. The Commissioner of Income-tax, Burma* (1).

The petitioners were assessed for the year 1925-26 and on appeal from the Income-tax Officer, the Assistant Commissioner of Income-tax enhanced their assessment by a very considerable amount. The Commissioner confirmed this enhancement and the petitioners then, on a reference made by him to this Court, sought the opinion of the Bench on five points of law. Their success was not conspicuous, but on the fourth question placed before the Court the Bench showed them some indulgence. On page 122 of the aforementioned report, the Judgment said:—"Our answer to question 4, therefore, is that if the enhancement of the Assistant Commissioner is based on materials from which he could reasonably conclude, though only as a rough estimate, that two lakhs of rupees was the income of the Moulmein business, then the enhancement was legal; if, on the other hand, the enhancement was wholly arbitrary and based on no materials, it was illegal. In view of this answer, the proper course for the Commissioner to adopt will be to call upon the Assistant Commissioner to give the grounds on which he based his assessment and the Commissioner as an appellate tribunal can then consider whether the enhancement is justified on these materials. If in his opinion there were materials on which the Assistant Commissioner could arrive at the enhanced figures, there is an end of the matter, since there is no further appeal and we cannot enter into questions of fact, namely, as to the sufficiency of those materials for the conclusion arrived at."

Acting on this direction of the Bench, the Commissioner called upon the Assistant Commissioner to give his reasons in detail for the enhancement of the assessment. The Assistant Commissioner did so in a report and the petitioners were heard on the consideration of this report by the Commissioner. The report was upheld and the order of the Commissioner approving the enhancement is before us as an exhibit marked "C". It is a very short order and merely finds as a fact that there were ample materials, on which the Assistant Commissioner could arrive at the conclusions he did in relation to the increase in the petitioners' liability.

On the petitioners asking for a reference to this Court from the Commissioner on various points of law alleged to have arisen under his confirming order, the Commissioner refused to admit their petition, as in his view it did not arise from an order under section 31 or section 32 of the Act. He used these words:—"The order against which it is directed is a revisional order passed in pursuance of the High Court's order under section 66 (5) of the Act." It is thus that a petition for mandamus reaches us.

It was argued on behalf of the petitioners that this hearing before the Commissioner was not a revision but an appeal by reason of the language stated above from the Bench judgment. It was further contended that in all appeals the appellate tribunal has a duty to consider fully the matters before it and to give reasons for coming to any conclusion. It was also argued before us that the Bench's action in referring back to the Commissioner and its direction that the Assistant Commissioner should give his detailed reasons for enhancing the

(1) 4 I. T. C. 111.

assessment was action taken under sub-section (4) of section 66. Sub-section (4) runs as follows:—"If the High Court is not satisfied that the statements in a case referred under this section are sufficient to enable it to determine the question raised thereby, the Court may refer the case back to the Commissioner by whom it was stated to make such additions thereto or alterations therein as the Court may direct in that behalf."

On the other hand, it will be seen from the Commissioner's letter to the petitioners refusing to state a case in the present proceedings that he took the view that the action of the Bench was not taken under sub-section 4, but under sub-section 5. Sub-section 5 runs as follows:—"The High Court upon the hearing of any such case shall decide the questions of law raised thereby, and shall deliver its judgment thereon containing the grounds on which such decision is founded, and shall send to the Commissioner by whom the case was stated a copy of such judgment under the seal of the Court and the signature of the Registrar and the Commissioner shall dispose of the case accordingly, or, if the case arose on a reference from any Income-tax authority subordinate to him, shall forward a copy of such judgment to such authority who shall dispose of the case conformably to such judgment."

The language employed in the Judgment of the Bench is not altogether clear, but in my opinion the intention of the Bench is quite easy to appreciate. The words, for example, "if in his opinion" that is, the Commissioner's opinion, "there were materials on which the Assistant Commissioner could arrive at the enhanced figure, there is an end of the matter, since there is no further appeal and we cannot enter into questions of fact" show a plain indication that the petitioners are precluded from further appeal.

Although the circumstances of the case are a little out of the ordinary, I think the Bench intended to proceed under sub-section 5, section 66 and not under sub-section 4. The Commissioner was wrong in heading his confirmation as a revision; it was in reality a referred appeal without further recourse to this Court but that is of little consequence.

The whole difficulty has arisen owing to the initial action of the petitioners in suppressing the proper material on which the officers of Government could arrive at a fair assessment. In my view the present application should be dismissed with costs in favour of the Crown, seven gold mohurs.

CARR, J.:—I concur in the decision proposed.

I am clearly of opinion that the Commissioner of Income-tax was wrong in basing his refusal of a reference on the ground that his finding was one arrived at in revision. Section 66 (5) of the Act requires the Commissioner to "dispose of the case" in accordance with the judgment of the Court. Here "the case" can mean only the case out of which the reference arose, in this instance the appeal before the Commissioner. When, therefore, the Commissioner proceeded to consider and decide the question of fact which he had previously left undecided and which the Court said that he ought to decide he was proceeding in the appeal. The decision at which he arrived was such as not to affect his original final order in the appeal, but had his decision been different it would have become necessary to re-open the whole appeal and to pass a fresh final order in it.

But that is merely a technical question and when we come to consider the merits I am equally clearly of opinion that there was no question of law which the Commissioner could have referred, or which this Court can require him to

refer. The whole burden of the petitioners' complaint is in fact that the Commissioner has not set out in detail the grounds on which he held that there were ample materials on which the Assistant Commissioner's assessment could be based. It is contended that on general principles it is the duty of an officer deciding an appeal to set out fully the considerations which have led him to his decision. But the Act itself gives no directions on the subject and it seems to me, therefore, a matter of propriety rather than of law, and thus a matter with which this High Court has no concern. Let us suppose, for example, that the Commissioner had set out in detail his reasons for arriving at this finding of fact, and that the petitioner had based his present application on a contention that those reasons were inadequate and unsound. It would be quite clear then that, the question being one of fact, the Court could not have considered the reasons set out. The Court has no jurisdiction to consider the findings of fact arrived at by an Income-tax authority and it is immaterial whether the grounds stated for those findings are sound or unsound, or whether no reasons at all have been stated. Thus no question of law arises and the Court has no jurisdiction in the matter.

(376) IN THE HIGH COURT OF JUDICATURE AT PATNA.

Before Mr. Justice James and Mr. Justice Chatterji.

(16th May, 1930).

Lalit Kishore Mitra

.. Assessee.

vs.

The Commissioner of Income-tax, Bihar and Orissa.

Indian Income-tax Act (XI of 1922) Secs. 23 (4) and 66 (2) and (3)—Non-submission of return—Sufficiency of cause therefor not accepted—Summary assessment—Question, if one of law—Assessment, if illegal.

On an assessment under Sec. 23 (4) of the Income-tax Act for non-submission of return, the assessee unsuccessfully applied to the Income-tax Officer under Sec. 27 to re-open the assessment on the ground that his son entrusted with the preparation of the return forgot it on account of marriage preparations. On the dismissal of an appeal therefrom to the Assistant Commissioner and an application to the Commissioner under Sec. 66 (2), the assessee applied to the High Court for a case to be stated.

HELD, that there was no point of law for a reference and that the summary assessment, though larger than the previous years' assessments could not be said to be based on no evidence or so arbitrary in its nature as to be illegal.

Application [Miscellaneous Judicial No. 50 of 1930] under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) for an order to direct the Commissioner of Income-tax, Behar and Orissa, to state a case for the opinion of the High Court.

Jayaswal, Subal Chandra Mazumdar and N. N. Roy, for the Assessee.

C. M. Agarwala, for the Crown.

JUDGMENT.

JAMES, J.:—The petitioner failed to submit a return in accordance with a notice issued under the provisions of section 22 (2) of the Income-tax Act; and his assessment was made summarily under section 23 (4) of the Act. He applied under section 27 of the Act stating grounds for his failure to submit his return, but the reasons were not found to be sufficient by the Income-tax Officer and his petition was rejected. An appeal to the Assistant Commissioner was dismissed, whereupon the petitioner applied to the Commissioner to state a case under section 66 (2) of the Income-tax Act. This application was also rejected.

Mr. Jayaswal on behalf of the petitioner argues in the first place that he has shown sufficient cause for his failure to submit his return under section 22 (2) of the Act, and in the second place that the summary assessment was arbitrary and therefore illegal. The reason given for the failure to file the return was that the petitioner's son, who was entrusted with the responsibility of preparing it, forgot the matter owing to the fact that his father had entrusted him with the arrangements for the marriage of the petitioner's grand-daughter. The Income-tax Officer and the Assistant Commissioner considered this reason to be inadequate, and it certainly cannot be said, as a point of law, that they were not justified in their view. The summary assessment was larger than the assessment of 1927-28 which was made on the basis of the petitioner's returns; but it cannot be said that the assessment was based on no evidence, or that it was so arbitrary in its nature as to be illegal. The application must accordingly be rejected with costs. Hearing fee two gold mohurs.

CHATTERJI, J.:—I agree.

(377) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt., Chief Justice, Justice Sir C. C. Ghose, Kt.,
and Mr. Justice Buckland.*

(16th May, 1930).

Raghunathdas Sewlal

.. Assessee.

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Indian Income-tax Act (XI of 1922), Secs. 22 (2), (4) and 66 (2) and (3)—Notice to produce accounts after submission of return, Legality of—Reference application to Commissioner—Question framed one month after appellate order—Rejection as time barred.

A notice under Sec. 22 (4) of the Income-tax Act for production of account books issued after the submission of a return of income by the assessee is valid.

Where after the hearing of the application under Sec. 66 (2), a supplementary question of law was submitted to the Commissioner who refused to refer it as filed more than a month after the passing of the order of the Assistant Commissioner and hence time-barred,

HELD, that the question was out of time, having regard to Sec. 66 (2) of the Act and was rightly refused reference by the Commissioner.

Case [Income-tax Reference No. 11 of 1929] stated under Sec. 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal in compliance with the order of the High Court dated 16th January, 1928.

CASE.

In pursuance of the order of Court, I have the honour to refer under section 66 (3) of the Income-tax Act the following case for the decision of the Hon'ble High Court.

2. The following are the facts of this case:—Messrs. Raghunath Das Sewlal, hereafter called the ‘Assessee,’ having their offices in Calcutta, are dealers in piece goods, sugar, jute, gunny and hessian, observing the Ramnavami year ending in April as their year of account. On the 29th of May, 1926, a notice was issued upon them by the Income-tax Officer, District IV (1) Calcutta, calling for a return of their income during the previous year, viz., Ramnavami, 1982, by the 30th July, 1926. On 31st July, 1926, a petition was filed asking for one month's extension of time. This was allowed. On the 21st August, 1926, another petition was filed praying for two months' time on the plea that the books could not be adjusted owing to the absence of the Gomosta who had gone to his native village. Time was allowed till the 24th September, 1926. On the 30th September, 1926, another petition came in for a further two months' extension on the same plea as before. But time was refused as the Income-tax Officer considered that more than ample time had already been granted. On the 1st October 1926, he issued a notice under section 22 (4) calling for books of Ramnavami, 1982 and 1981 for 7th November, 1926. On the 8th November, 1926, the assessee submitted their return showing a loss of Rs. 39,206. Thereupon, the Income-tax Officer issued a combined notice under sections 23 (2) and 22 (4) of the Act requiring the assessee to produce any evidence on which they might rely in support of the return, and also accounts of three years 1980, 1981, and 1982 Ramnavami on the 19th November, 1926. On this date they only produced the accounts of their cloth business and not of any other business and those for 1982 Ramnavami only. The case was then adjourned to 23rd November, 1926, when the assessee were asked to produce three years' books for all the Departments of their business as mentioned in the notice under section 22 (4). On the 23rd November, 1926, a petition was filed asking for a fortnight's time on the plea that the accountant was ill and so there was none to explain the accounts. The Income-tax Officer granted time till the 27th November, 1926. On the 27th November, 1926, the assessee produced Jamabahi, Nakal and Rokar of the hessian business only for 1982 Ramnavami, but not even the ledger of this business, not to speak of the accounts of the other businesses which they had been asked to bring on that day. The assessee put forward the plea that the previous years' accounts had been sent to Bikaner, but no explanation was given as to why they were sent, nor was any evidence produced that they were sent there. The Income-tax Officer therefore did not accept this statement holding that it had no foundation in fact. On the same plea they filed a petition on the 30th November, 1926, asking for twenty days' time for production of all the books called for. This was rejected. However, for some reason the case was not taken up till the 23rd December, 1926, when a fresh combined notice under sections 22 (4) and 23 (2) issued for production of evidence in support of the return as well as the accounts of the three years for the 12th January, 1927. As the Christmas holidays intervened this notice was served on 5th January, 1927. The assessee did not pay any heed to the notice. In the circumstances the assessment was made under section 23 (4) on the 15th January, 1927.

3. On the 27th January, 1927, the assessees presented a petition under section 27 on the ground that they were prevented by sufficient cause from complying with the requisitions under sections 23 (2) and 22 (4).

4. On the 12th February, 1927, they filed a supplementary petition under section 27 stating that the notice under section 23 (2) was complied with by production of accounts on the 23rd November, 1926 and 27th November, 1926, only the ledger of the hessian business was not brought through mistake, and that on the 12th January, 1927, their pleader appeared and applied for a fortnight's adjournment on the ground that the head gomosta, who was the only person competent to explain the accounts had gone to Gangasagore for pilgrimage. Further the accounts of 1980 and 1981 could not be produced having been detained at Bikanir and a long time would be required for their production.

5. On the 14th February, 1927, the Income-tax Officer rejected the petition on the ground that none of the notices had been fully complied with, and sufficient time had been granted for compliance and that the pleader appeared before him on the 12th January, 1927, after he had passed the order, but as no petition for time was filed before him he did not take action.

6. The Assistant Commissioner of Income-tax upheld this decision on appeal. Before him a new plea was put forward to explain the non-production of books of 1980 and 1981, to the effect that they were sent to Bikanir in connection with a Civil suit. As no proof of this was forthcoming he did not accept the plea. He passed his order on the 23rd February, 1927.

7. From the above account it is obvious that the assessees had more than 7 months' time from the date of the service of the notice under section 22 (2) till the date of the assessment to produce complete accounts of the previous year, and I hold that there was no object in examining the books as produced in their incomplete state since no reliable estimate of income could have been arrived at from these incomplete books. It is also clear that they wilfully withheld the books of the two years immediately anterior to the previous year as had they been at Bikanir in connection with a Civil suit, as was alleged before the Assistant Commissioner of Income-tax for the first time, the requisition of the Bikanir Court could have been produced before him. Moreover, it was stated in the subsequent petition under sections 33-66 (2) that the decree of the Bikanir Court would be produced at the time of the hearing of that petition but this promise was never fulfilled. The only evidence produced before the Commissioner was two affidavits sworn by Gomostas, but they were not accepted as proof in the absence of any other evidence.

8. The books were no doubt rightly requisitioned since it is not possible to arrive at a correct computation of the income of a business like that of the assessees from the books of the previous year only. These have to be tallied with books of the earlier years to see whether stocks have been rightly carried forward.

9. Subsequently they filed a petition under section 33-66 (2) for review of the Assistant Commissioner's order, or in the alternative for a reference to the High Court of certain questions of law. After the hearing of this petition the counsel of the assessees submitted on the 2nd May, 1927, a supplementary question of law which ran as follows:—"If a potential assessee has made a return in pursuance of a notice under section 22 (2) and thereafter a notice has been served upon him under section 23 (2) and also a notice under section 22 (4) and the potential assessee has complied with all the terms of the notice under

section 23 (2), but has failed to comply with the notice under section 22 (4), is the Income-tax Officer entitled to refuse to examine the evidence produced in pursuance of the notice under section 23 (2) and to make an assessment under section 23 (4), or is he bound to proceed under section 23 (3)."

10. It is not a fact as stated in the assessee's petition before the High Court that my predecessor who heard the section 33-66 petition asked their counsel "to formulate more explicitly a pure question of law involved in the questions of law, which are already mentioned in the said petition" (petition under section 33-66 (2)). He (my predecessor) refused to refer this supplementary question to the High Court on the grounds (1) that it was filed on the 2nd May, 1927, after the lapse of one month of the passing of the appellate order by the Assistant Commissioner on the 23rd February, 1927, and was time-barred, and (2) that it was based on a mis-statement of fact as the notice under section 23 (2) was not fully complied with. He refused to state the other questions on the ground that no question of law arose.

11. Thereupon the assessee's moved the Hon'ble High Court under section 66 (3) of the Act and the Court issued a Rule upon me to show cause why I should not refer the following questions to it with my own opinion for the opinion of the Court:—(1) Whether the notice under sub-section (4) of section 22 of the Indian Income-tax Act of 1922 upon the assessee's therein mentioned to produce their account books was valid, having regard to the fact that the said assessee's had made a return of their income; (2) if not, whether the Income-tax Officer in the said petition mentioned was entitled to proceed to assess them under sub-section 4 of section 23 of the Indian Income-tax Act, and (3) whether the application made by the said assessee's to the said Income-tax Officer and mentioned in the said petition was out of time having regard to sub-section 2 of section 66 of the said Income-tax Act.

12. On reconsideration of my predecessor's order I decided to state a case and the Rule was accordingly made absolute.

13. I now refer the questions with my opinion which is as follows:—As regards questions (1) and (2) I submit that in view of the circumstances of this case the notice under section 22 (4) was valid, and the Income-tax Officer rightly made the assessment under section 23 (4) for failure to comply with the notice. This is the view which the Hon'ble High Court expressed in the case of *Harmukhrai Dulichand v. The Commissioner of Income-tax, Bengal* (1). As regards question 3, I submit that the Hon'ble High Court appear to be referring to the question of law, filed on the 2nd May, 1927, in connection with the application under section 66 (2) before my predecessor, as no petition to the Income-tax Officer was held to be out of time. According to section 66 (2) I am only authorised to refer to the High Court any question of law, arising out of the appellate order under section 31 or 32, which the assessee's may file within one month of the passing of such order. In this case the Assistant Commissioner passed his order in appeal on the 23rd February, 1927 and the question of law was filed on the 2nd May, 1927. In the circumstances I am of opinion that the question was out of time, having regard to sub-section (2) of section 66 of the Income-tax Act (XI of 1922).

JUDGMENT.

RANKIN, C. J.:—In this case, the questions of law must be answered in favour of the Income-tax authorities. The first question is already covered by

decision. The second question does not arise and on the third question the Commissioner of Income-tax appears to be right. In my judgment these questions should be answered accordingly and the assessee must pay the costs of this Reference.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

(378) IN THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

Before Mr. Justice Mukerji and Mr. Justice Bennet.

(16th May, 1930).

Seth Kasinath Bagla

.. Assessee.

v.

The Commissioner of Income-tax, United Provinces .. Referring Officer.

Indian Income-tax Act (XI of 1922) Secs. 23 (4), 33 and 34—Assessment under Sec. 23 (4)—Additional assessment of escaped income—Actual income found less than original assessment—Jurisdiction to revise original assessment on appeal—Proceedings under Sec. 34, scope and limits of—Commissioner's review powers.

Where an assessment under Sec. 23 (4) of the Income-tax Act was enhanced under Sec. 34 and on appeal the Assistant Commissioner finding the actual income to be less than the original assessment set aside the additional assessment but refused to reduce the original assessment and give the appropriate refund,

HELD, that the provisions of Sec. 34 limit the action of the Income-tax authorities, the Income-tax Officer and the Assistant Commissioner, to the assessment of income previously escaping assessment or assessed at too low a rate, with no jurisdiction to revise the original assessment or to make a new assessment and grant relief on that basis.

Whether in this case the Commissioner could exercise the discretion under Sec. 33 in favour of the assessee is a matter solely for him and not a matter for the High Court to consider in a reference.

P. L. M. Palaniappa Chettiar v. The Commissioner of Income-tax, Madras.
4. I. T. C. 196; Adopted.

Case [Miscellaneous Case No. 46 of 1930] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, United Provinces, for the opinion of the High Court.

CASE.

The assessee in this case is a Hindu undivided family represented by a minor, said to be a person of unsound mind, under the guardianship of his mother. The family was assessed to income-tax and super-tax in 1926-27 on an income of Rs. 1,17,600, and the assessment was made under section 23 (4) of the Indian Income-tax Act, 1922, because no return of income was filed.

2. In the following year the Income-tax Officer had reason to believe that the full income of the family had not been assessed and he accordingly issued a notice under section 22 (2) read with section 34 of the Act calling for a return of income with a view to the assessment of the income which had escaped assessment. A return was filed and the Income-tax Officer assessed the income of the family at Rs. 1,31,875. An appeal was filed and the Assistant Commissioner differing from the Income-tax Officer, found that the actual income was less than had been originally assessed under section 23 (4). He therefore cancelled the additional assessment made under the proceedings initiated in pursuance of the provisions of section 34 but refused to reduce the original assessment made under section 23 (4) and by means of such reduction to give a refund of the proportionate amount of the tax paid in that year.

3. The assessee now claims a reference to the High Court on the following grounds:—

- “(1) Whether in a case where original assessment proceeded on an estimate merely under section 23 (4) and later on the Income-tax Officer revised the proceedings and enhanced the income by making an assessment under section 34 on the basis of account books in an absolutely different and original manner, the Assistant Commissioner of Income-tax was precluded from allowing the appeal in full and from granting relief to the assessee, even though he is satisfied beyond doubt that a grave injustice had been done to him, for the simple reason that it would involve a refund of the tax to him.
- (2) Whether the Income-tax authorities have no inherent power to set right a flagrant injustice by ordering refund of the whole or a portion of the tax originally assessed in proceedings in appeal under section 34 of the Income-tax Act.
- (3) Whether it is not a case where the Commissioner in exercise of the powers vested in him under section 33 of the Income-tax Act, should grant refund *ex gratia* because the strict operation of the law would entail great hardship.
- (4) Whether the Income-tax authorities having set the machinery for assessment in motion by issuing notice under section 34 Income-tax Act, are not bound to take the consequences and whether they are not precluded from withholding a refund if the attempted additional assessment results in a refund.”

4. The meaning of the second question propounded by the assessee is not clear. Income-tax authorities exercise certain powers under the Income-tax Act but have not been invested with any dispensing power. If, however, the assessee means that in this particular case the Assistant Commissioner should have taken action under some specific section of the Act the question is virtually covered by the first and fourth questions.

5. The third question does not arise out of the appellate order and raises a question of the exercise by the Commissioner of a discretion vested in him. The Commissioner, therefore, does not state this question for the decision of the High Court. In passing it may be remarked that the Commissioner can only exercise his functions within the provisions of the Income-tax Act and has no dispensing power as the term *ex gratia* used by the assessee seems to imply.

6. The first and fourth questions are in essence identical and the Commissioner would state the points as follows:—(a) Do the provisions of section 34 limit the action of the Income-tax authorities to the assessment of income which has previously escaped assessment or which has been assessed at too low a rate; or (b) do they confer on those authorities a power of revision of a previous assessment and if the revision results in showing that the assessment under section 23 (4) was too much, can relief be granted to the assessee?

7. The above statement of the facts has been accepted by the assessee, and the points of law which are stated in the foregoing paragraph are those which after discussion the advocate of the assessee desires to be stated for the decision of the High Court.

8. In the opinion of the Commissioner the answer to part (a) of the portion in para. 6 is in the affirmative and to part (b) in the negative.

JUDGMENT.

This is a reference by the Commissioner of Income-tax on the application of an assessee who is a minor of unsound mind under the guardianship of his mother. On the 2nd February, 1927 the Income-tax Officer made an assessment under section 23 (4) of the Indian Income-tax Act, acting under that section because no return of income had been filed. The assessment was on an income estimated at Rs. 1,17,600 and the minor was assessed to income-tax and super-tax, the assessment being based on the income estimated for 1925-26. On 11th March, 1928 the Income-tax Officer came to the conclusion that some income had escaped assessment and accordingly he issued a notice to the minor under sections 22 (2) and 34 for the same year's income. Accounts were filed and the Income-tax Officer assessed the income as Rs. 1,31,875. Against that assessment of extra income an appeal was made to the Assistant Commissioner and the Assistant Commissioner held that the actual income was less than the Rs. 1,17,600 which had been originally assessed on the 2nd of February, 1927. It is admitted that he did not proceed to find what in his opinion the total income was, but he treated the matter before him as confined to the appeal against an assessment on additional income and he accordingly allowed the appeal.

The assessee has now asked that an opinion should be given as to whether the Assistant Commissioner was precluded from granting relief to the assessee against the original assessment under section 23 (4). This is the main point in the case. Now section 34 under which the second notice was issued states as follows:—If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year, or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

We consider that the words in the later part of the passage quoted "assess or re-assess such income, profits or gains" must be taken to refer to the income, profits or gains chargeable to income-tax which have escaped assessment referred to in the prior part of the section. Accordingly in a proceeding under section 34 the Income-tax Officer and after him the Assistant Commissioner are only dealing with the extra income which has not been assessed to income-tax. No jurisdiction

is given to either of these Officers by section 34 to make a new assessment for the purpose of taxing the whole of that assessment under the Income-tax Act. Accordingly our answer to the first question "Do the provisions of section 34 limit the action of the Income-tax authorities to the assessment of income which has previously escaped assessment or which has been assessed at too low a rate?" is in the affirmative. We hold that the Assistant Commissioner of Income-tax was precluded from granting any further relief to the assessee than allowing his appeal against the assessment of extra income-tax. We may note that this opinion is in accordance with an opinion of a Full Bench of the Madras High Court in *P. L. M. P. L. Palaniappa Chettiar v. Commissioner of Income-tax, Madras* (1).

The second question is whether section 34 confers on the authorities "a power of revision of a previous assessment and if the revision results in showing that the assessment under section 23 (4) was too much can relief be granted to the assessee?" As already stated we consider that this question must be answered in the negative.

A further question was put forward by the assessee as to whether the Commissioner could exercise his discretion in his favour under section 33 of the Act. The question of the exercise of his discretion by the Commissioner is a matter solely for the Commissioner and not a matter for this Court to consider in a reference.

No further question arises on this reference. Accordingly we direct that the reference be returned with these answers.

As the applicant has not succeeded in his application, we direct that he should pay his own costs and the costs of the Government including the fees of the Government Advocate assessed at Rs. 100.

(379) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt., Chief Justice, Justice Sir C. C. Ghose, Kt.,
and Justice Sir Philip Buckland, Kt.*

(16th May, 1930).

Messrs. Haridas Premji

Assessee.

v.

The Commissioner of Income-tax, Bengal.

Referring Officer.

*Indian Income-tax Act (XI of 1922), Sec. 2 (14)—Registration of firm—
Letters between partners containing terms—If registrable as instrument of
partnership.*

*Where an application for registration of a firm under Sec. 2 (14) of the
Income-tax Act on the basis of letters addressed by the junior partners to the
senior partner setting out the shares and certain other stipulations and the
latter's reply, was rejected by the Income-tax Officer on the ground that there was*

no instrument of partnership but merely letters and multiplicity of documents, while the Commissioner refused to accept them as the senior partner's reply did not purport to accept all the terms proposed by the junior partners,

HELD, that the Income-tax Officer's grounds for rejection were erroneous and that the proper course was to get the junior partners to write another letter waiving the other terms and conditions not accepted by the senior partner, or the latter to write accepting them and to treat the registration application so amended as made in good time on the date of the original application.

Case [Reference No. 10 of 1929] stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

I have the honour to refer the following case for the decision of the Hon'ble High Court under section 66 (2) of the Income-tax Act.

2. The following are the facts of this case. Messrs. Haridas Premji, an unregistered firm hereinafter called the assessee, are merchants dealing in cotton yarn and keeping the Dewali year as their year of account. The partners are Premji Ramji, who is the senior partner, Haridas Gokuldas and Tulsidas Nanji having 7 annas, 5 annas and 4 annas shares, respectively. In compliance with a notice under section 22 (2) they submitted a return of their income on the 15th July, 1928, showing an income of Rs. 2,500 during the accounting year 1928 Dewali. Subsequently they made an application for registration of their firm accompanied by copies of four letters, viz., one by each of the junior partners addressed to the senior partner, and one by the senior partner addressed to each of the junior partners, which they contended amounted taken together to an instrument of partnership. The Income-tax Officer, however, held that these letters could not constitute an instrument of partnership as contemplated by Rule 2 of the Income-tax Rules. Accordingly he refused the application for registration, and made the assessment on the assessee as an unregistered firm on the 30th August, 1928. On appeal the Assistant Commissioner upheld the decision of the Income-tax Officer.

The assessee has now asked me, in the event of my declining to interfere in the revision, to refer the following question of law for the decision of the Hon'ble High Court: "Whether the documents produced by your petitioners constitute an instrument of partnership under section 2 (14) of the Indian Income-tax Act." The question is in a sense a question of fact but appears to contain an element of law as well.

I have declined to interfere in revision, and so refer the question with my opinion, which is as follows:—

The above-mentioned letters, which are in Guzrati, were produced before the Income-tax Officer, and a translation of them was attached to the petition of appeal.

Now assuming the said translation to be correct, it appears that in the first two letters the junior partners Haridas Gokuldas and Tulsidas Nanji, who were apparently at the time employees in the shop of Premji Ramji, proposed certain terms of partnership to the latter. There are 16 clauses in each of the letters which are in identical

terms. Clauses 2, 3 and 4 propose what shares each of the 3 should have in the firm. Clauses 5 to 15 propose a variety of other conditions such as that the two junior partners should be allowed to draw Rs. 75 for their household expenses which should be debited to their accounts, that at dewali time each year accounts should be adjusted and profits or losses should be credited or debited to the respective accounts of the partners, that the junior partners should manage the business in consultation, etc., etc. Clause 16 says that the deed has been executed by the junior partners willingly, with full sense and not under the influence of drink and that they are bound by it.

Now, if in the last two letters Premji Ramji had referred to the first two letters and had clearly accepted all the conditions of partnership proposed to him by the other two, it might perhaps have been said that the four letters taken together amounted to a valid instrument of partnership, which the Income-tax Officer might have acted upon after the assessee had paid the necessary stamp duty and penalty under section 35 of the Stamp Act. As it is, however, Premji Ramji in the last two letters does not refer to the first two letters at all, and simply says he will give the other two 5 annas and 4 annas shares respectively, that is the shares proposed by them in their letters, for working as long as they work in his shop. He says nothing about any of the other conditions. It seems to me an essential condition of a genuine partnership that all the partners should accept all the conditions of the partnership. In this case there is nothing to show whether Premji Ramji, the senior partner, accepted the greater part of the conditions proposed by the junior partner, or not. In the circumstances, I am of opinion that the letters in question do not amount to an instrument of partnership for the purpose of Rule 2 of the Indian Income-tax Rules.

JUDGMENT.

RANKIN, C. J.:—In this case, it appears that there is a certain firm and that firm has three partners. It is apparently a shop and it has been going on in the name of Haridas Premji. The question is with regard to the assessment of income-tax for the year of assessment 1928-29. There is no dispute between the Income-tax authorities and the assessee as to the amount of the profits or gain; but the assessee was minded to claim to be taxed as a registered firm. Accordingly, they in time filed an application in the prescribed form to be registered on the basis of certain letters passed between the three partners. It appears that the two junior partners were intended to be working partners and that the capital was to belong entirely to the senior partner and the profits were to be divided 7 annas to the senior partner Ramji Premji, 5 annas to Haridas Gokuldas and 4 annas to Tulsidas Nanji. The letters which the two junior partners addressed to the senior partner set out the shares and set out certain other stipulations. The letters which the senior partner addressed to the junior partners were simply this: "I agree to give you 5¼ annas share for working as long as you work in my shop No. 71, Cross Street which is carried on in the name of Haridas Premji and in this share I shall not raise any objection."

Now, the Income-tax Officer and the Assistant Commissioner refused to register these documents upon the ground that they were letters and multiplicity of documents and not an instrument of partnership as required by sub-section (14) of section 2 of the Act. That point of view is conceded by the learned Advocate General to be erroneous and it was not upheld when the matter was

taken before the Commissioner of Income-tax. The reason, however, why the Commissioner of Income-tax has thought that he cannot accept these documents for registration under the Act is that the reply of the senior partner does not purport to accept all the terms proposed by the junior partners. It accepts the term as regards the amount of the shares of the profits but it is silent as to a number of the matters that were proposed in the letters addressed to the senior by the juniors. That being so, no doubt there does arise a question of some difficulty because one then has to enquire whether something which did not purport itself to be an agreement was in fact an agreement by reason that the actings of the parties had contributed assent to the documents which do not appear by themselves to have been consented to.

It appears to us that the reasonable course, in which the learned Advocate General concurs, is this; that either the junior partners should write another letter saying that the other conditions proposed by their letters to the senior partners are waived, or that the senior partner should write another letter to the junior partners saying that the other terms and conditions proposed by them are accepted by him. We are of opinion that that is the proper course which should be adopted in this case; and it will be understood in view of the fact that the point taken by the Income-tax Officer and the Assistant Commissioner is really a different point, that this Court is of opinion that the application when amended by the addition of this further document is to be treated as the same application and as made in good time on the date on which the original application was made. Our intention is that it should govern this particular assessment. That being so, our answer to the question "whether the documents produced by your petitioners constitute an instrument of partnership under section 2 (14) of the Income-tax Act" will be in this form: In our opinion, this question does not at the present stage arise because, in view of the position adopted by the Income-tax Officer and the Assistant Commissioner, the assessees should be allowed to file an additional letter clearing up the ambiguity noticed by the Commissioner of Income-tax in the case stated before us. There will be no order as to costs in this reference.

GHOSE, J.:—I agree.

PATTERSON, J.:—I agree.

(380) IN THE HIGH COURT OF JUDICATURE AT CALCUTTA.

*Before Sir George Rankin, Kt., Chief Justice, Justice Sir C. C. Ghose, Kt.,
and Justice Sir Philip Buckland, Kt.*

(16th May, 1930).

Martin and Co.

.. Assessees.

v.

The Commissioner of Income-tax, Bengal

.. Referring Officer.

Indian Income-tax Act (XI of 1922)—Partners carrying two businesses—Single assessment on joint income, legality of—Businesses, if different partnerships—Factors determining the question.

Under agreements entered into in February 1927 between the partners of M. & Co., and the partners of B. & Co., the business of B. & Co., was purchased

by the former who thereafter continued it separately under the old name. The general accounts of the partners in M. & Co., the monies therein being the firm's working capital as well as the partner's private property, were debited with the purchase price which was credited to a special account "B. & Co. purchase account", amounts being paid thereout to B. & Co.'s partners. For the year 1927-28 M. & Co., submitted a return of their income with an application for registration, while B. & Co. claimed to be assessed separately as an unregistered firm. The Income-tax Officer held that the proprietors of the two concerns being identical there was only one firm, M. & Co., for purposes of assessment, B. & Co. being a branch business and treating the registration of M. & Co. as covering both the concerns, included the income of B. & Co., in M. & Co.'s assessment.

On a reference to the High Court, the Court held that the question to be determined by the Commissioner was whether in substance and in truth the partners as part of the business of M. & Co., bought up certain assets, (in which case the fact that these assets went by a different name would have no importance whatever), or whether it was an entirely separate venture not intended to be any part of the business of M. & Co. or to have any connection with it, (it may be composed of the same partners and it may be that the partners were interested in the same shares but as a matter of intention of the parties, an entirely different partnership) and referred the case back to him for further findings under Sec. 66 (4) of the Income-tax Act.

The Commissioner found that in view of no separate account being opened in M. & Co.'s books treating B. & Co. as an asset and the purchase price having been provided out of the private property of the individual partners, the intention of the partners was to embark on a separate venture unconnected with the business of M. & Co. On the case coming up again with these additional findings the Court held that B. & Co. must be assessed separately as an unregistered firm.

Case [Reference No. 6 of 1929], stated under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal, for the opinion of the High Court.

CASE.

At the request of the assessee, Messrs. Martin and Company, I have the honour to refer under section 66 (2) of the Income-tax Act, XI of 1922 to the Hon'ble High Court certain questions of law which have arisen out of the order of the Assistant Commissioner of Income-tax, Calcutta, on the appeal filed by them against the assessment made on them for the year 1927-28.

The following are the facts of the case:—Messrs. Martin and Company are a registered firm within the meaning of section 2 (14) of the Income-tax Act. The partners of the firm are (1) Sir R. N. Mukherjee, (2) Messrs. T. L. Martin, (3) H. P. Martin, (4) O. S. Martin, (5) C. W. Walsh, (6) P. N. Banerjee and (7) J. N. Mukherjee. These seven partners purchased the business of Messrs. Burn and Company under the provisions of 2 agreements dated the 26th January, 1927 and the 1st February, 1927 respectively. On the 18th February, 1927 the partners of both the firms executed a partnership agreement providing for the retirement of the old partners of Burn and Company as from the 2nd February, 1927 and the carrying on of the business of the firm of Burn and Company from that date by the purchasers, viz., the partners of Martin and Company. This document was supplemented by another document dated the 28th September, 1927 dealing with the shares of the partners of Martin and Company in the profits

of Burn and Company and other partnership matters. Neither of these 2 latter documents were registered under section 2 (14) of the Act. The partnership deed of Martin and Company was however so registered.

The shares held by each of them in Martin and Company are identical with those owned by them in Burn and Company. Thus in the year of assessment, *viz.*, 1927-28, they were collectively owners of both the concerns and as such assessable to tax in respect of the income of Burn and Company under section 26 of the Act, on the basis of the Privy Council ruling in the case of the *Western India Turf Club, Limited v. Commissioner of Income-tax, Bombay*(1). On the 24th September, 1927, Messrs. Martin and Company submitted a return of their income but did not include therein the income of Burn and Company, who submitted a separate return of income on the 24th August, 1927 in compliance with a notice under section 22 (2) issued to them on the 16th April, 1927. This separate notice was issued to them evidently because the Income-tax Officer did not know that Burn and Company had become the property of Martin and Company. Messrs. Martin and Company did not deny their liability to pay the tax which would have been paid by their predecessors in interest on the income of Burn and Company. On the other hand they contended that the two concerns are separate entities, and that separate assessments should be made on their incomes. The application for renewal of registration was made for Martin and Company only, as the intention was that Burn and Company should be separately assessed as an unregistered firm. The Income-tax Officer did not accept this contention, holding that the proprietors of the two concerns being identical, the two must be considered to be one firm for purposes of assessment, as the same person cannot possess two separate entities from an income-tax point of view even though he may own more than one business. In renewing the registration of Martin and Company for the year 1927-28 he regarded such registration as covering both concerns. He therefore included the income of Burn and Company in Martin and Company's assessment, considering that Burn and Company was not a separate firm at all but only a branch of Martin and Company's business.

Objecting to the assessment assessee filed an appeal before the Assistant Commissioner of Income-tax, Calcutta, on the following amongst other grounds: (1) The firm of Burn and Company is an unregistered firm within the meaning of section 2 (16) of the Income-tax Act. (2) The firm of Burn and Company forms no part of the assets of Martin and Company, but represents the investment of the private monies of certain of their partners, and so Burn and Company should have been assessed separately as an unregistered firm.

The Assistant Commissioner of Income-tax did not accept any of the above grounds and upheld the assessment.

Being dissatisfied with the Assistant Commissioner's order they subsequently petitioned me to revise it, or in the alternative to make a reference to the High Court on the following questions of law: (a) For the purposes of the Act can the income of a registered and an unregistered firm be aggregated and taxed as a whole, or (b) Does the Act provide that a registered firm and an unregistered firm shall be treated as separate and distinct legal entities for the purpose of taxation and be assessed accordingly? and (c) Does the fact that the individuals interested in the profits of both concerns are the same affect this position?

I have declined to interfere on revision under section 33 of the Act and accordingly refer the above mentioned questions of law with my opinion which is as follows:—

Before questions (a) and (b) can arise it is to be decided whether there are actually two firms in question. The Income-tax Officer and the Assistant Commissioner held that there is only one firm, *viz.*, Messrs. Martin and Company of which the concern known as Messrs. Burn and Company must be held to be a branch business. In this view I concur. It is therefore not a fact that the incomes of a registered and an unregistered firm were taxed as one as is implied by these questions. I would have refused to refer these questions, as in their present form any question of law which might have been held to arise is based on something in the nature of a misstatement of fact, had it not been that there is a question of law underlying the questions as framed, and that is whether in the circumstances of the case the concerns are to be treated as two separate firms for income-tax purposes or not. My opinion in regard to this question is, as already expressed, that since the acquisition of Messrs. Burn and Company by Messrs. Martin and Company or, to say the same thing in different words, by the partners of the latter Burn and Company has merged in Martin and Company, though for trade purposes the old name of the former may have been retained. As such the aggregate income of the two businesses must be taxed as one under section 3 of the Act. So far as the Income-tax Act is concerned a business which has merged in another business in the manner described cannot retain a separate legal entity.

Question (c) is easily answered. The fact that the individuals interested in the profits of both concerns are the same vitally affects the issue, as otherwise there would have been no question of a single assessment being made on the total profits of both businesses combined.

The case coming on for hearing, the Court delivered the following judgment on the 25th June, 1929 remitting the case back to the Commissioner of Income-tax for supplemental findings.

JUDGMENT.

RANKIN, C. J.:—In order to dispose of the questions referred to us, it is necessary that we should refer the case back to the Commissioner to make certain additions thereto or alterations therein as provided by clause (4) of section 66 of the Income-tax Act of 1922. The observations which I propose to make now are entirely directed to making clear, so far as I can, the points upon which further findings are required at the hands of the Commissioner.

It appears that there is a firm called Messrs. Martin and Co. which is governed by certain Articles of Partnership in writing. There seem to be three such documents. These documents have not been made part of the case stated. They ought to be made part of the case stated. It is not exactly clear to me whether as a result of these three documents that firm is shown to have had 7 partners or only 5. The documents will make that matter clear. In 1927, certain persons bought a business which was being carried on under the name and style of Burn and Company. From the documents which have been made part of the case, it would rather appear that the persons who bought that business were 5 in number, and it would further appear that these 5 persons became partners for a day at least with the original proprietors of the firm of Burn and Company. The terms upon which, the original proprietors having gone, the new proprietors were carrying on the business are defined in the document dated the 1st February, 1927 by a reference to the documents which govern the firm of Messrs. Martin and Company. The words "so far as applicable to this present partnership" appear in the document of 1st February, 1927. That is a matter which has not been discussed by the Commissioner in the case stated at all. That

matter ought to be dealt with. He ought to give any facts in his judgment bearing upon the question as to the weight to be given to that reference in clause (3) of the agreement of the 1st February, 1927.

Again, in the document of the 28th September, 1927 which is an agreement to which the five purchasers to whom I have referred are parties, I find that in clause (4) two other people are suddenly described as partners. It seems to be necessary that it should be ascertained how that comes about. At the end of that clause, there is a statement to the effect that these two gentlemen being the senior assistants are entitled in pursuance of the partnership deed of Messrs. Martin and Company to participate in the net profit of Burn and Company. The Commissioner ought to consider that, upon the question whether or not in substance and in truth the assets which had belonged to Burn and Company were being bought by the firm of Martin and Company, or whether in substance and in truth there was an entirely different firm (it may be composed of the same partners and it may be that the partners were interested in the same shares but as a matter of intention of the parties, entirely different partnership). The Commissioner has not found whether there is or is not truth in the statement which appears to have been the case of the assessee, that the firm of Burn and Company was bought not with any funds belonging to the firm of Martin and Company at all but with other funds being the private property of the individual persons who were partners of Messrs. Martin and Company. A finding as to that is very necessary.

In remitting the case to the Commissioner, I would point out not by way of deciding this case but entirely for the guidance of the Commissioner that this case may ultimately have to be decided upon findings which do not at present appear in the case stated. The proposition that the same persons in the same shares cannot for income-tax purposes be partners of two entirely separate firms is a highly abstract proposition. It may or may not be correct but I am not prepared as at present advised to proceed upon so very general a principle without a careful enquiry into the concrete case and into the matters above mentioned. It may turn out that the case depends on the question of fact whether the two firms were entirely separate, a question of fact including the question of intention. It is necessary that we should know whether in substance and in truth the partners as part of the business of Martin and Company bought up certain assets (in which case the fact that these assets went by a different name would have no importance whatever), or whether, on the other hand, it was an entirely separate venture not intended to be any part of the business of Martin and Company or to have any connection with Martin and Company. If the fact is that certain persons—be they 5 or 7 put their hands in their pockets to buy the assets of Burn and Company with the intention of running a firm which would have nothing to do with Messrs. Martin and Company, then the Commissioner should in justice to the assessee give a finding to that effect. Looking upon it in that way, it seems to me desirable that this case should be sent back to the Commissioner to make such additions thereto or alterations therein as are required to meet the points which in this judgment I have mentioned.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

SUPPLEMENTARY CASE.

With reference to the order of the Hon'ble High Court on the 25th June 1929, asking me under section 66 (4) of the Income-tax Act, XI of 1922 to give my findings in respect of certain points mentioned therein, I have the honour to

submit the following additional facts in continuation of the reference made in my letter No. 18997-C. T., dated the 16th March, 1929.

2. The firm of Messrs. Martin and Co., as now constituted is governed by three partnership documents, which are (1) a deed of partnership dated 6th December, 1919, in which, besides stating the main conditions of partnership, it is declared that the partnership shall continue for a term of five years from 1st January, 1921, (2) a memorandum, dated 20th March, 1923, modifying certain clauses in the deed of partnership, and (3) a memorandum, dated 19th November, 1925 renewing the partnership for another five years from 1st January, 1926. The copies of the three partnership documents are submitted as enclosures to this letter.

3. Clause 10 of the deed of partnership, dated 6th December, 1919 shows that there are seven parties to the indenture, viz., (1) Sir R. N. Mukherjee (2) Mr. O. S. Martin (3) Mr. T. L. Martin (4) Mr. M. P. Martin (5) Mr. C. W. Walsh (6) Mr. J. N. Mukherjee (7) Mr. P. N. Banerjee of whom the first five gentlemen are apparently regarded by the firm as the real partners, the last two being regarded as assistants rather than partners, though, in view of the fact that they participate in the profits and losses of the business and contribute their share of the capital, it would seem that their legal liability is that of partners.

4. As a result of the agreements, dated the 26th January, 1927 and the 1st February, 1927 between the former partners of Messrs. Burn and Company and the first five gentlemen mentioned above, the latter became partners together with the former in the firm of Messrs. Burn and Company on the first February, 1927, and, the original partners of Burn and Company having retired on the 2nd February, 1927, the five gentlemen in question became the sole partners of the firm of Burn and Company on and from that date. Going by the documents alone it would seem as if the above mentioned five partners of Martin and Company purchased the business of Burn and Company and that at the outset Messrs. J. N. Mukherjee and P. N. Banerjee took no share in the purchase. That Messrs. Mukherjee and Banerjee, whose names do not appear in the agreements of 26th January, 1927 and 1st February, 1927, having to do with the purchase of Burn and Company, were parties to the purchase of Burn and Company from the outset is, however, shown by the fact that (1) their general accounts were debited along with the general accounts of the five partners on the 1st February, 1927, with their share of the 52 lakhs, the purchase price of Burn and Company, and (2) they each of them on the 4th February, 1927, wrote letters (copies enclosed) addressed to the five partners of Martin and Company approving of the terms and conditions of the purchase of Burn and Company and agreeing to be liable for their share of the losses, if any, of Burn and Company in consideration of their receiving a like share of the profits of Burn and Company as they were receiving in respect of the profits of Martin and Company.

5. An agreement subsequent to the agreements of the 26th January, 1927, and the 1st February, 1927 was drawn up by the aforementioned five gentlemen on the 28th September, 1927, in which they agreed to give the two senior Assistants of Martin and Company (J. N. Mukherjee and P. N. Banerjee as mentioned above) one anna share each in the firm of Burn and Company as they had been given in the firm of Martin and Company subject to the conditions imposed on them in the partnership deed of Martin and Company, dated the 6th December, 1919.

6. The phrase "so far as applicable to this present partnership" appearing in clause 3 of the agreement, dated the 1st February, 1927, signified that the

deed of partnership in the case of Martin and Company did not apply to that of Burn and Company in all respects. For example (1) according to clause (1) of the agreement dated the 28th September, 1927 supplementary to the partnership agreement dated the 1st February, 1927, of Burn and Company the value of the goodwill of Burn and Company was fixed at a sum representing the total net profits over a period of three years as compared with one year's profits in clause 26 of the partnership agreement of Martin and Company, dated the 6th December, 1919, (2) the capital in Martin and Company is 4 lakhs per share (*vide* clause 7 of the partnership deed), while there is no fixed capital in Burn and Company (*vide* clause 3 of the supplementary agreement of the 28th September, 1927), (3) the two firms have different accounting years, Martin and Company closing on the 31st December, (*vide* clause 20 of the deed of partnership) subsequently altered to the 30th September and Burn and Company closing on the 30th April, subsequently altered to the 31st July.

7. The accounts of Martin and Company show that the first five partners of Martin and Company have two accounts each—one capital account proper which shows the minimum amount which each of them is bound to contribute to the capital of the firm in accordance with clause 7 of the partnership deed of the 6th December, 1919, and one general or drawing account to which the partner's profits from the firm are credited and his losses and drawings debited, while Messrs. Mukherjee and Banerjee have only a general account each. The latter two gentlemen's general accounts include, besides their profits from the firm, the minimum amount which he is bound to contribute to the capital of the firm under clause 7 of the partnership deed of the 6th December, 1919. The amount of capital included in the five capital accounts remains constant from year to year.

8. The purchase price of Burn and Company (*vide* clause 2 of the agreement of the 26th January, 1927), was at first fixed at 50 lakhs, but later a further asset of Burn and Company, *viz.*, the Managing Agency of the Indian Standard Waggon Company was included in the assets sold, and the purchase price was raised to 52 lakhs (*vide* agreement, dated the 1st February, 1927).

9. The entries recording the purchase appear in the books of Messrs. Martin and Company as follows:—The general accounts of the partners and two senior assistants of Martin and Company were individually debited with their respective proportions of the purchase price and a special account headed "Burn and Company Purchase Account" credited with Rs. 52 lakhs thereby transferring the whole of the purchase price from the individual partners of Martin and Company to Messrs. Burn and Company. The first portion of the purchase price namely Rs. 42 lakhs was paid on the 1st February, 1927, by a cheque of Martin and Company in favour of Messrs. Orr Dignam and Company, the Solicitors to Messrs. Burn and Company. The balance of Rs. 10 lakhs was subsequently paid to the 5 retired partners of Burn and Company direct in accordance with the terms of the Agreement of the 26th January, 1927, as to Rs. 5 lakhs on the 1st February, 1928 and as to the balance of Rs. 5 lakhs on the 1st February, 1929. The books of Messrs. Burn and Company were opened on the 1st February, 1927 with corresponding entries.

10. The fact that the general accounts of the five partners and two Senior Assistants of Martin and Company were debited with the purchase price of Burn and Company would not by itself necessarily indicate that the money with which Burn and Company was purchased was paid from the private funds of the seven persons in question, as the money in their General Accounts is admittedly the working capital of the firm, as well as their private property on which they draw interest from the firm at 6 per cent. (*vide* clause 7 of the partnership deed of the 6th December, 1919).

11. But the representative of Messrs. Martin and Company explains that if Burn and Company had been purchased by the firm of Martin and Company, an asset account would have been opened and Burn and Company would have been shown as an asset in Martin and Company's balance-sheet. My enquiries go to show that this is correct. It would also appear to be in accordance with the ordinary principles of accounting. It is a fact that no asset account was opened in the name of Burn and Company in Martin and Company's books, while their balance-sheet did not show Burn and Company as an asset. On the other hand Martin and Company's balance-sheet for the period ending 30th September, 1927 showed that the liabilities of the firm to the partners had been reduced by approximately 52 lakhs as compared with their liabilities at the end of the previous year ending 30th September, 1926.

12. The Hon'ble High Court has asked me to come to a finding of fact in regard to two points, *viz.*:—(1) Whether there is or is not truth in the statement that the firm of Burn and Company was bought, not with any funds belonging to the firm of Martin and Company at all, but with other funds being the private property of the individual persons who were partners of Messrs. Martin and Company; and (2) Whether in substance and in truth the partners as part of the business of Messrs. Martin and Company bought up certain assets (Burn and Company), or whether on the other hand it was an entirely separate venture not intended to be any part of the business of Martin and Company or to have any connection with Martin and Company.

13. In view of the facts given in paragraphs 9 and 11 of this letter, I am inclined to accept the statement referred to in point (1) as true.

As to point 2, after reviewing all the facts and considering the further materials that have been placed before me, I am of opinion that the intention was to embark on a separate venture, which should have no connection with the business of Messrs. Martin and Company.

FINAL JUDGMENT.

RANKIN, C. J.:—In this case, certain questions of law were referred to us by the Income-tax Commissioner and this Court, at the first hearing of the Reference on the 25th of June, 1929, made an order sending the case back to the Commissioner to make such additions thereto or alterations therein as were required to meet certain points indicated in the judgment. The Commissioner has accordingly sent to us an additional statement of facts and, on the main question between the parties, he has now found the facts in favour of the assessee. In these circumstances, it appears to me that the questions propounded to us should all be answered in favour of the assessee and the learned Advocate-General on behalf of the Income-tax authorities does not further press the Reference. The Income-tax authorities must pay the costs of the assessee on the previous occasion and on the present occasion.

GHOSE, J.:—I agree.

BUCKLAND, J.:—I agree.

PRIVY COUNCIL.

(381) ON APPEAL FROM THE COURT OF THE JUDICIAL
COMMISSIONER, NAGPUR.

PRESENT.

*Lord Tomlin, Sir Lancelot Sanderson, Sir George Lowndes
and Sir Binod Mitter.*

(19th May, 1930).

Maulana Mohammad Ibrahim Riza Malak .. Appellant.*
v.The Commissioner of Income-tax, Central
Provinces and Berar .. Respondent.*Indian Income-tax Act (XI of 1922), Sec. 4 (3) (1)—Atba-e-Malak-Badar
community—Income from property vested in Head—No specific trust for
charity—Exemption from assessment.**Income from properties vested in the Head of the Atba-e-Malak-Badar
community for purposes many of which were neither religious nor charitable and
not identified as appropriated exclusively for any charitable or religious purposes,
is not exempt from assessment under Sec. 4 (3) (1) of the Income-tax Act.*Appeal [Privy Council Appeal No. 50 of 1929] from a judgment of the
Court of the Judicial Commissioner, Nagpur, [Findlay, J. C. and Macnair,
A. J. C.] dated 4th August, 1927, reported as 2 I. T. C. 443.*A. M. Dunne and E. B. Raikes, for the Appellant.**DeGryther and Wallach, for the Respondent.*

JUDGMENT.

LORD TOMLIN:—In this case the appellant seeks to displace an assess-
ment to income-tax made upon him in respect of property vested in him as the
head of a community which is a sect of the Dawood Borah tribe, located at Nagpur.
The community have, apparently, a common stock, all the property being vested
in the head of the sect. The property is utilized in part in carrying on a series
of shops, the profits of the trade being treated as part of the income of the
community.

In the Courts below the appellant rested upon certain trust deeds executed,
one on the 25th August, 1917, and the other on the 25th November, 1922. By
the first deed the then head of the community declared the trusts of the property
vested in him, and by the second deed the trusts of the same property were
explained and expanded.

Their Lordships think that the short point which this appeal raises is,
whether, having regard to the terms of those deeds, the income of the property
vested in the head of the community is exempt from income-tax, having regard
to the provisions of section 4, sub-section 3 (i) of Act XI of 1922. That sub-
section of section 4 is in these terms:—"This Act shall not apply to the following
classes of income: (i) Any income derived from property held under trust or
other legal obligation wholly for religious or charitable purposes, and in the case
of property so held in part only for such purposes, the income applied or finally
set apart for application, thereto."

* 57 I. A. 260 ; 32 B. L. R. 1538 ; 59 M. L. J. 905 ; 33 L. W. 39 ; A.I.R. (1930) P. C. 226.

A glance at the documents on which the appellant has founded himself in the Courts below makes it plain that the income of the trust property is applicable to purposes, many of which are neither religious nor charitable. It is only necessary to refer to one or two of the clauses of the first deed to establish that proposition. Clause 3, which indicates some of the purposes for which the property is held is: "For carrying on the agricultural, industrial, commercial and other pursuits of the said community." Clause 5 is: "For entertaining guests, giving at homes or parties." Clause 6 is: "for such donations for charitable or religious purposes, contributions to memorials, funds raised for holding social, educational, religious, industrial or political conferences or congresses, and for public entertainments," as the then spiritual head, and, after him, the spiritual head for the time being, may deem fit. Their Lordships think that these extracts establish that the income is not "income derived from property held under trust or other legal obligation wholly for religious or charitable purposes." Nor is it suggested that any part of the property is set aside for any charitable or religious purposes, so that it can be identified as appropriated exclusively to such purposes.

In these circumstances the conclusion which has been arrived at by the Court below seems to their Lordships to be correct.

It perhaps is right to add that it was suggested that some comfort could be found by the appellant from a deed of the 9th June, 1894, in which certain property was vested in the then head of the community upon religious or charitable trusts; but no attempt has been made, either here or below, to identify the property, the object of that trust, with any of the property now said to be subject to tax. Their Lordships think that in the absence of any evidence of identity and having regard to the fact that throughout, in the Courts below, the later deeds only have been founded upon, it is not open to the appellant to assert before their Lordships' Board that the deed of the 9th June, 1894, has any relation to the matter.

In their Lordships' opinion the appeal must be dismissed with costs, and they will humbly advise His Majesty accordingly.

Solicitors for the Appellant: *T. L. Wilson and Co.*

Solicitors for the Respondent: *Solicitor, India Office.*

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